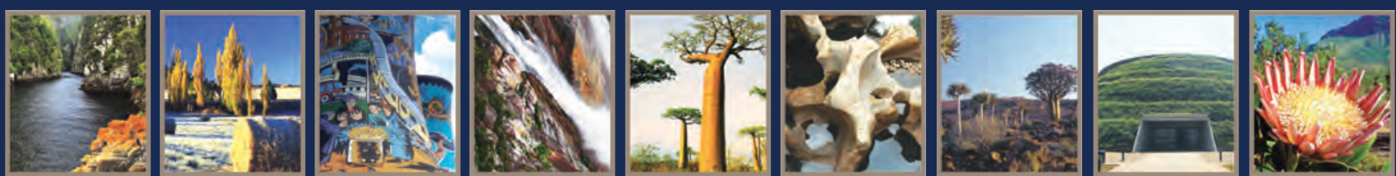
PFMA
2016-17



CONSOLIDATED
General report on national and provincial audit outcomes

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

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Auditing to build public confidence

PFMA 2016-17

CONSOLIDATED

General report on national and provincial audit outcomes

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 key legislation.

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 the national and 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 government.

Auditor-General

Kimi Makwetu
Auditor-General

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.

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ANNEXURES

The annexures containing information on the following are available on www.agsa.co.za (our website):

- **Annexure 1:** Auditees' audit outcomes; areas qualified; and findings on predetermined objectives, compliance, specific risk areas and unauthorised, irregular as well as fruitless and wasteful expenditure
- **Annexure 2:** Auditees' financial health indicators, SCM findings and root causes
- **Annexure 3:** Auditees' audit opinions over the past five years
- **Annexure 4:** Assessment of auditees' key controls at the time of the audit

A This icon is used in the report to refer to the annexures

To access the content of this report on our website, simply use the QR code scanner on your mobile phone or tablet to scan the code.

CLEAN AUDITS 2016-17

Unqualified financial statements with no material findings on the quality of the performance report or compliance with key legislation

NATIONAL

DEPARTMENTS

- Communications
- Government Communications and Information System
- Mineral Resources
- National School of Government
- Parliament of the Republic of South Africa
- Planning, Monitoring and Evaluation
- Public Enterprises
- Social Development
- Sport and Recreation South Africa
- Statistics South Africa
- Tourism
- Trade and Industry
- Traditional Affairs

PUBLIC ENTITIES

- Agricultural Land Holding Account
- Armaments Corporation of South Africa
- Banking Sector Education and Training Authority
- Boland TVET College
- Brand South Africa
- Buffalo City TVET College
- Chemical Industries Education and Training Authority
- Commission for the Promotion and Protection of the Rights of Cultural, Religious and Linguistic Communities
- Companies and Intellectual Property Commission
- Competition Commission
- Construction Education and Training Authority
- Council for Scientific and Industrial Research
- Council for the Built Environment
- Cross-Border Road Transport Agency
- Deeds Registration Trading Account
- Education, Training and Development Practices Sector Education and Training Authority
- Ekurhuleni East TVET College
- Ekurhuleni West TVET College
- Esayidi TVET College
- False Bay TVET College

- Fibre Processing Manufacturing Sector Education and Training Authority
- Financial Services Board
- Gammatec NDT Supplies
- Guardians Fund
- Health and Welfare Sector Education and Training Authority
- Independent Regulatory Board for Auditors
- Insurance Sector Education and Training Authority
- Land Bank Life Insurance
- Legal Aid South Africa
- Majuba TVET College
- Media, Information and Communication Technologies Sector Education and Training Authority
- Medical Research Council of South Africa
- Mintek
- National Agricultural Marketing Council
- National Consumer Tribunal
- National Energy Regulator of South Africa
- National Gambling Board
- National Lotteries Commission
- National Lottery Distribution Trust Fund
- National Nuclear Regulator
- National Youth Development Agency
- Nkangala TVET College
- NTP Radioisotopes
- Office of the Ombud for Financial Service Providers
- Office of the Pension Funds Adjudicator
- PetroSA Ghana
- Port Elizabeth TVET College
- Public Investment Corporation Limited
- Quality Council for Trades and Occupations
- Road Accident Fund
- Road Traffic Infringement Agency
- Road Traffic Management Corporation
- Robben Island Museum, Cape Town
- South African Civil Aviation Authority
- South African Human Rights Commission
- South African Local Government Association
- South African National Biodiversity Institute
- South African National Energy Development Institute
- South African Tourism
- Special Investigating Unit
- State Diamond Trader

EASTERN CAPE

DEPARTMENTS

- Provincial Treasury
- Rural Development and Agrarian Reform
- Safety and Liaison

PUBLIC ENTITIES

- East London Industrial Development Zone Corporation
- Eastern Cape Parks and Tourism Agency
- Eastern Cape Rural Development Agency

FREE STATE

DEPARTMENTS

- Provincial Legislature
- Provincial Treasury

PUBLIC ENTITIES

- No public entity in the Free State achieved a clean audit

GAUTENG

DEPARTMENTS

- Cooperative Governance and Traditional Affairs
- Economic Development
- e-Government
- Office of the Premier
- Provincial Legislature
- Provincial Treasury
- Social Development

PUBLIC ENTITIES

- Gauteng Enterprise Propeller
- Gauteng Growth and Development Agency
- Gauteng Partnership Fund
- Gautrain Management Agency
- Supplier Park Development Company

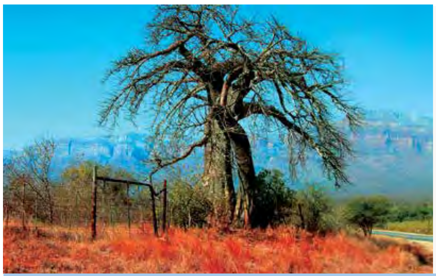
KWAZULU-NATAL

DEPARTMENTS

- Provincial Treasury
- Sport and Recreation

PUBLIC ENTITIES

- Dube Tradeport Company
- KwaZulu-Natal Sharks Board



LIMPOPO

DEPARTMENS

- Provincial Treasury

PUBLIC ENTITIES

- Limpopo Gambling Board

MPUMALANGA

DEPARTMENS

- Co-operative Governance and Traditional Affairs
- Economic Development and Tourism
- Provincial Treasury

PUBLIC ENTITIES

- Mpumalanga Gambling Board

NORTHERN CAPE

DEPARTMENTS

- Environment and Nature Conservation
- Office of the Premier
- Provincial Legislature
- Provincial Treasury

NORTH WEST

DEPARTMENTS

- Provincial Treasury

PUBLIC ENTITIES

- No public entity in North West achieved a clean audit

WESTERN CAPE

DEPARTMENTS

- Community Safety
- Cultural Affairs and Sport
- Economic Development and Tourism
- Education
- Environmental Affairs and Development Planning
- Local Government
- Office of the Premier
- Provincial Parliament
- Provincial Treasury
- Social Development
- Transport and Public Works

PUBLIC ENTITIES

- Government Motor Transport
- Saldanha Bay IDZ Licencing Company
- Western Cape Gambling and Racing Board
- Western Cape Housing Development Fund
- Western Cape Nature Conservation Board
- Western Cape Tourism, Trade and Investment Promotion Agency

1 Executive summary

1. Executive summary

As the electoral term of the current government moves into its last year, this report reflects on the progress made since 2014 in the financial and performance management of national and provincial departments and public entities. Our message is aimed at the public accounts committees and portfolio committees in Parliament and the provincial legislatures who have very little time left to strengthen the legacy of accountability and impactful oversight they had envisaged. This report is further aimed at the political and administrative leadership who has set great and worthy targets in the Medium-term Strategic Framework (MTSF) to improve the lives of citizens and who will account for what has been achieved in the period and if money had been spent on its intended outcome. Hence, the central theme of this report is **accountability for government spending: from the plan to the people**.

In order to demonstrate the importance of accountability for government spending and the impact of poor financial and performance management on the delivery of key programmes of government, we include our findings on the **management and delivery of five key programmes included in the estimates of national expenditure** (ENE) for 2016-17, namely water infrastructure development, expanded public works programme, school infrastructure, food security and agrarian reform, and housing development finance, which combined had a budget of R58,5 billion. The programmes either **did not achieve the targets highlighted in the ENE or did not report on whether targets had been achieved** even though the allocated budgets had been spent. Where **grants** were given to provincial departments, the spending and achievement of targets **for some of the programmes were not adequately monitored**. Accounting for the expenditure, liabilities and assets related to the programmes was not always credible and resulted in **qualifications in the financial statements of departments**, especially where the departments used implementing agents to manage projects. **Irregularities in procurement processes and inadequate contract management** were common – again more so when implementing agents were used. Although using implementing agents are often the most effective way of delivery, the departments did not adequately manage and correctly account for the projects executed by these agents. Some of the projects funded through these programmes displayed serious weaknesses in terms of **delayed delivery, poor quality work, and mismanagement**. We reported all of this to the accounting officers. This is also not the first year we have reported these matters to the ministers, members of the executive councils and portfolio committees – we have provided performance reports, sector reports, audit reports and special briefings highlighting these weaknesses.

The accountability for government spending at state-owned enterprises (SOEs) is an area receiving attention in the public, as government funds and guarantees are being used to sustain some of the SOEs. The **audit outcomes of SOEs continued to regress** – most often as a result of inadequate controls, monitoring and oversight. Of the 25 SOEs we report on, only five received clean audit opinions in 2016-17 and the audits of six were still outstanding – four in the South African Airways (SAA) group, SA Express and the Independent Development Trust. The audit outcomes of the SOEs audited by private audit firms also regressed. Instability at board and executive level played a role in the outcomes of SOEs. The level of oversight by the departments the SOEs report to differed and there was no single approach in this regard. The political leadership was also inconsistent – at some SOEs there was a high level of involvement, while at others the required decision-making and policy direction were not adequate.

The number of **SOEs with irregular expenditure** decreased slightly but the value increased significantly to R2 884 million, of which the Airports Company South Africa (Acsa), South African Post Office (Sapo) and South African Broadcasting Corporation (SABC) were the main contributors. The reason for this was the increased weakening of supply chain management (SCM) at SOEs – although SCM policies were in place, we found that officials were not familiar with the policies and the procurement processes they should follow, and in some cases circumvented the processes. Of most concern and impact are that the **financial health of SOEs regressed**. For just over a quarter of them, there was significant doubt on whether they could continue their operations in future – these included the SABC, the Sapo group, and the Petroleum Oil and Gas Corporation (PetroSA). We are also concerned about the losses incurred and other concerning financial indicators at the Armaments Corporation of South Africa (Armscor), the South African Nuclear Energy Corporation (Necsa), and the Land and Agricultural Development Bank of South Africa (Land Bank) group.

Our concerns with regard to government spending also extend to the financial health of auditees and in particular the national and provincial departments. Since 2013-14, there has been a **regression in the overall financial health of departments**. The 46% of departments with good financial health represents only 36% of departmental budgets, and the number of departments in financial difficulty almost doubled over the four-year period. Overall, there is an emerging trend of departments failing to manage their finances properly. Some departments did not pay their creditors when their budgets started running out and thereby avoided unauthorised expenditure, but the payments then happened in the following year, effectively using money intended for other purposes. Some departments overspent on their budgets and still had outstanding liabilities at year-end. This continuing 'rollover' of budgets had a negative impact on departments' ability to pay creditors on time and to deliver services. The education and health departments were affected the most in this regard and their inability to deliver services will have an impact on the most vulnerable in society. The signs of financial failure at the departments in the Free State should receive urgent attention. Furthermore, a **going concern uncertainty** existed at 15 of the public entities (excluding SOEs) in 2016-17 – a slight increase since 2013-14 and 2015-16.

Over the past four years, there have been **improvements in the audit outcomes but at a very slow rate**. The number of auditees that improved is often offset by those that regressed and most of the auditees (103 departments (65%) and 91 public entities (50%)) had the same audit outcomes as in 2013-14 – of which only 57 had a clean audit opinion. If only the improvements to clean audits were sustainable, the proportion would have been much higher – a third of the auditees that obtained clean audits in 2013-14 regressed in 2016-17. In 2016-17, the improvements were limited – departments showed a slight regression and public entities a slight improvement. Although it is encouraging that the **number of clean audits increased** to 126 from 85 in 2013-14, this represents only 30% of the auditees and 10% of the total 2016-17 budget.

By 31 August, **26 audits** (6%) **had not been completed** – an increase from the 13 audits that had not been completed at the same time last year. The main reasons for this were the late or non-submission of financial statements and outstanding information. Nine of the audits were outstanding as a result of public entities in the SAA group and some in the transport and public enterprises portfolio attempting to resolve their going concern status.

The trend of **contestations to our audit findings** continued and intensified in 2016-17 and led to the delay of some audits. It is acceptable for auditees to question and challenge the outcome of audits, based on evidence and solid accounting interpretations or legal grounds. We also acknowledge that many of the accounting and legal matters dealt with in the audits are complex and often open to interpretation. But at some auditees, pressure is placed on audit teams to change conclusions purely to avoid negative audit outcomes or the disclosure of irregular expenditure – without sufficient grounds. This is done by threatening legal action and the increased use of lawyers to dispute even accounting matters as well as attacks against the motives and methods of our audits. There were also cases of personal threats and intimidation. Often ministers, members of the executive councils and premiers get involved. The leadership should take accountability for poor audit outcomes and irregular expenditure and work on improvements, and not try to coerce the auditors into changing their conclusions.

The **Western Cape and Gauteng continued to produce the best results** – with 85% and 52% clean audits, respectively. The improvement made year-on-year was mostly sustainable. Common in both provinces was the role of the leadership in instilling a culture of accountability and expecting nothing less than sound administration. Members of the executive councils and provincial treasuries have a common goal of clean administration and, under the leadership of the premiers, are working systematically towards that goal in spite of facing similar challenges as the other provinces.

The audit outcomes of the **Eastern Cape improved** by 38% over the past four years to 29% clean audits, with only the education department still struggling to move from a qualified opinion. The provincial treasury played a significant role in these improvements through not only responding to our recommendations but actively seeking our advice. However, the province continued to be plagued by poor SCM practices and project and service delivery failures – for which there were little accountability and consequences.

There were also noticeable **improvements in Limpopo** in the past four years – moving from 13 auditees with qualified, adverse and disclaimed audit opinions to eight auditees with qualified opinions and two with clean audits. Improvements can be attributed to the **political leadership taking accountability and discharging oversight responsibility through robust discussions and interrogating reports** submitted by the administrative leadership. The premier **honoured his commitment** to improve audit outcomes and to hold the executive leadership accountable for the outcomes.

The **outcomes in Mpumalanga, the Northern Cape and KwaZulu-Natal were erratic** over the past four years – improvements in the one year were offset by regressions in the following year. A lack of urgency by the leadership in honouring commitments and implementing action plans and a slow response to applying consequences were some of the root causes of these erratic outcomes.

A **lack of accountability and commitment towards clean administration was evident in North West and the Free State**. Their audit outcomes regressed over the four years – the Free State showed a slight improvement in 2016-17 but North West is in a downward spiral. The response by the provincial leadership was to contest the audit conclusions instead of addressing the weak control environment at most of the auditees.

At **national departments and public entities,** there was a slight improvement in outcomes (41 improved and 31 regressed), and the number of clean audits increased to 30%. Half of the national auditees that received adverse, disclaimed or qualified opinions were technical and vocational education and training (TVET) colleges.

The departments of **education, health and public works** that are responsible for almost 38% of the budget and for implementing key programmes to improve the health and welfare of citizens, continued to have the poorest outcomes – 40% of these departments received qualified opinions compared to only 16% of the other departments. Only two of the departments in these sectors received clean audit opinions.

The outcomes in the three main areas that we audit are as follows:

- In total, **77%** of the auditees where we completed our audits received unqualified audit opinions. The number of auditees with unqualified **audit opinions on the financial statements slightly improved** from 266 to 305 over the four-year period. However, departments regressed from the previous year – mostly as a result of the incorrect accounting for implementing agent agreements and the value of buildings being audited for the first time. Auditees continued to **rely on auditors** to identify material misstatements to be corrected. Only 53% (rather than the reported 77%) of the auditees would have received an unqualified audit opinion had we not identified the material misstatements and allowed them to make corrections. Nevertheless, the quality of the financial statements submitted for auditing has been improving every year – from 38% in 2013-14 to the current 53%.
- The number of auditees with **no material findings on the quality of their performance reports increased slightly over the four-year period but regressed from the previous year** to stand at **61%**. Only 34% would have had this positive outcome had we not identified the material misstatements and allowed them to make corrections. The usefulness of the information in these reports continued to improve, but the main stumbling block towards quality reporting is the reliability of the information – at 33% of the auditees, the reported achievements were incorrect or we could not audit the achievements as evidence could not be provided to support them.
- The audit area that showed the **most improvement was the compliance with key legislation,** with the auditees with no material findings in this regard increasing from 25% to 36%. However, this still means that almost two-thirds of the auditees materially did not comply with key legislation. The lapse in oversight and controls in the area of compliance was evident in a number of areas, including SCM that led to increased irregular expenditure.

Irregular expenditure had increased by 55% since the previous year to R45,6 billion. The amount could be even higher, as it does not include the irregular expenditure of the auditees where the audits are still ongoing – including the Passenger Rail Agency of South Africa (Prasa) where the irregular expenditure last year was almost R14 billion. Furthermore, 25% of the auditees disclosed that they had incurred irregular expenditure but that the full amount was not known, while 28 auditees were qualified as the amount they had disclosed was incomplete. The top 10 contributors to irregular expenditure were responsible for 53% of the total amount of irregular expenditure – four of which were departments of health. As also reported last year, procurement by implementing agents was often the reason for the irregular expenditure, while grant money was used at six of the top 10 contributors. This links back to our concerns about the monitoring of projects funded by grants and the risks associated with using implementing agents.

The irregular expenditure does not necessarily represent wastage or means that fraud was committed – this needs to be confirmed through investigations to be done by the accounting officer or accounting authority – but losses could already have arisen or may still arise if follow-up investigations are not undertaken. The track record of auditees in **dealing with irregular expenditure** and ensuring that there is accountability is poor. The year-end balance of irregular expenditure that had accumulated over many years and had not been dealt with (through recovery, condonement or write-off) was R81 billion.
The significant increase can be **attributed overall to continued weaknesses in SCM.** The most common findings for the past four years related to **deviations from the prescribed procurement processes**. Three written quotations or competitive bids were not invited to enable the selection of a supplier based on a competitive and fair process. Although such deviations are allowed, we found that it had often not been approved; or, if approved, the deviation was not reasonable or justified. This points to the inappropriate use of management discretion in the procurement process. In some instances, the accounting officers used their discretion to appoint targeted suppliers without justifiable reasons – thereby failing to ensure compliance with legislation.

The Preferential Procurement Regulations make provision for the **promotion of local production and content.** These regulations are aimed at supporting socio-economic transformation. In 2015-16, we reported non-compliance with the regulations at 20 auditees and committed to increase our audit focus on this important government initiative. In 2016-17, we identified non-compliance at 39 auditees (43% of those where we audited this area) – these auditees demonstrated a **lack of understanding and awareness** of the requirements and even a disregard for them, which could result in government not achieving the objectives of this initiative.

There had been no improvement in addressing the concerns we have raised year after year about **contracts being awarded to employees and their families without the necessary declarations of interest**. Last year, we reported 2 548 instances of suppliers submitting false declarations of interest as part of the procurement processes, but 47% of the auditees did not investigate any of the cases we had reported to them; this year, we reported 1 699 instances. Instances of employees not declaring interests had an even lower investigation rate, with 68% of the auditees not investigating any of the cases.

Although there is no legislation that prohibits making awards to suppliers in which state officials have an interest, the **amended Public Service Regulations prohibit employees of departments from doing business with the state** from 1 August 2016. The regulations allowed employees that were doing business with the state on 1 August 2016 time until February 2017 to stop the business or resign as an employee. We found that 698 employees at 24 departments took no action in this transitional period and continued doing business with the state. In addition, 649 employees at 32 departments secured new awards after 1 August 2016, even though it is now prohibited. The onus of complying with these regulations is on the employees of departments, but departments have a responsibility to enable and monitor such compliance. Based on the findings in just the first six months of implementation, it seems that this responsibility is not being given the attention it deserves.

Fruitless and wasteful expenditure was 6% lower than in the previous year at R1 023 million. **Unauthorised expenditure** has steadily decreased since 2013-14 but increased by 93% from the previous year to R1 467 million.

Most auditees have the required policies and processes to ensure that transgressions and fraud are identified and acted upon, but chose not to use it – a clear indicator of a lack of commitment to accountability. Of the 99 auditees we audited where there were allegations of financial and SCM misconduct and fraud, a third did not investigate the allegations and at 32% investigations took longer than three months. The SCM findings we reported to management in 2015-16 for investigation were not attended to at a third of the auditees where we had reported it. Just over 20% investigated only some of the findings. As long as the political leadership, senior management and officials do not make accountability for transgressions a priority, irregular, unauthorised and fruitless and wasteful expenditure as well as fraud and misconduct will continue. An environment that is weak on consequence management is prone to corruption and fraud, and the country cannot allow money intended to serve the people to be lost.

There was **little improvement over the four years in the internal controls** at auditees in the key areas of leadership, financial and performance management, and governance. The area of **vacancies and stability showed improvement** in all key positions except for that of the chief executive officer – by the end of 2016-17, 21% of the public entities did not have a chief executive officer. **Information technology (IT) controls** should ensure the confidentiality, integrity and availability of state information, enable service delivery and promote security in national and provincial government. Although the status of IT controls had improved over the four years, we assessed that only 17% of the auditees had good IT controls, with continued focus needed in the areas of security management, user access management and IT continuity. IT-related expenditure increased by 56% in the last two years at departments due to revitalisation and modernisation projects, but the performance monitoring processes of service providers were not at the required level. Various project and governance weaknesses plagued the large IT projects in government, including the integrated financial management system (IFMS) project.

A key driver of the audit outcomes was the inadequate assurance provided by the different role players. The **assurance provided** by senior management, accounting officers and authorities, executive authorities and public accounts committees remained at low levels with only the latter two assurance providers showing improvement over the past four years, while the assurance provided by coordinating/monitoring departments regressed. Although internal audit units, audit committees and portfolio committees had the highest assurance levels, little progress had been made in the past year and their impact on audit outcomes was not always apparent, mostly as a result of management not implementing their recommendations.

In this report, we propose the use of the **'plan+do+check+act' cycle** (as illustrated in figure 1) to continuously improve the processes, outcomes and services of departments and public entities and thereby strengthen accountability.

Figure 1: Plan+do+check+act cycle

We provide a number of recommendations to contribute to this improvement process, of which the main ones are outlined below:

PLAN: Spend sufficient time and consult widely to clearly **define the targets** that should be achieved by the auditees in terms of audit outcomes, service delivery (including project delivery and infrastructure maintenance) and financial health using, among other, audit action plans, strategic and annual performance plans, annual budgets, and project plans. These targets should be specific, measurable, achievable, relevant and time bound. **Responsibilities** for achieving the targets should be allocated and **sufficient time and resources** should be provided to ensure that performance is managed through robust internal control and strong financial management.

DO: Good **internal control** is the key to ensuring that auditees deliver on their priorities in an effective, efficient and economical manner, produce quality financial statements and performance reports, and comply with applicable legislation – especially in the area of procurement and contract management.

It is the responsibility of accounting officers and authorities, senior managers and government officials to implement and maintain effective and efficient systems of internal control; hence, it is crucial that the **key positions** are filled with people with the required competencies. Stability in these positions also correlates with good audit outcomes. Auditees with poor audit outcomes should strengthen their financial and performance management systems through ensuring that the **basics** for a good internal control environment are in place, namely effective leadership, audit action plans, proper record keeping, daily and monthly disciplines, and the review and monitoring of compliance.

CHECK: A key element of internal control is **monitoring** by the different assurance providers to ensure that internal controls are adhered to, risks are managed, and outcomes are achieved. It is important that all the assurance providers understand their roles, are equipped to perform their functions and are given the authority their role requires; while the outcomes of their monitoring and oversight should also be responded to appropriately.

ACT: Accountability means that those performing actions or making decisions are answerable for them, but also that there should be consequences for transgressions, a lack of action and poor performance. Auditees should implement **consequence management** for officials who fail to comply with applicable legislation, while appropriate and timely action must be taken against transgressors. A less tolerant approach should be followed by all parties, including those charged with governance and oversight, which will result in accountability being enforced and consequences instituted against those who intentionally fail to comply with legislation.

Leading up to the finalisation and launch of this report, **engagements** took place countrywide. Accountability featured as a prominent element of these engagements and we trust that all those concerned will act on their commitments.

At this time, there is a lot of attention on the role of auditors and their ethical responsibility to report on irregularities and mismanagement. We have been reporting without fear or favour on poor financial and performance management, irregularities and transgressions – often repeating the same message year after year. In the public sector, the auditors are not always heard and our messages are not acted upon. In this last year of administration, we call on oversight to give attention to this report and ensure that there is accountability for government spending.

My office remains committed to working tirelessly within our mandate to strengthen financial and performance management in national and provincial government in South Africa, emphasising the need to do the basics right.

NOTES

2 Introduction

2. *Introduction*

As mentioned in the executive summary, this report reflects on the progress made since 2014 in the financial and performance management of national and provincial departments and public entities in this last year of the electoral term of the current government. At the centre of our message is **accountability for government spending: from the plan to the people**.

The political leadership and accounting officers and authorities who are entrusted with the accountability of state resources for the benefit of society, must achieve the objectives set for their departments and public entities, while acting in the public interest at all times and consistently adhering to the requirements of legislation and government policies. Accountability and good governance are central to building an efficient, effective and developmental-oriented public service. Accountability means that the leadership are answerable to the public and take responsibility for their actions, decisions and policies. These concepts of public interest and accountability are entrenched in the country's constitution and the legislation that governs national and provincial government.

The MTSF is government's strategic plan for the 2014-19 electoral term. It reflects the commitments made in the election manifesto of the governing party, including the commitment to implement the National Development Plan (NDP). The MTSF sets out the actions government planned to take and the targets to be achieved. It also provides a framework for the plans of national, provincial and local government. In this report, we provide our assessments and recommendations on the financial and performance management required to achieve these targets and improve audit outcomes by using the **'plan+do+check+act' cycle**. This cycle, also known as the Deming cycle, is used courtesy of the International Organization for Standardization. It is a repetitive, four-stage approach for continually improving processes, products and services, which forms a solid foundation for leadership accountability.

In section 3, we report on the **management and delivery of five key programmes of government** to demonstrate the importance of accountability for government spending. We also highlight where the management of these programmes should be enhanced to improve delivery to the people. The focus of section 4 is on **SOEs** that are showing signs of poor accountability and are having a significant impact on government spending. The theme of accountability for the financial management of auditees continues in section 5, which deals with the **financial health of departments and public entities**. The remainder of our report includes similar information and insights as in our 2015-16 report but with enhanced messages on accountability linked to the plan+do+check+act cycle.

It is important for us to share at the introduction of this report, the increasingly hostile environment in which we conduct our audits. In 2015-16, we reported that we experienced **contestation from auditees and their leadership** where they disagreed with our findings and conclusions. This trend continued and intensified in the 2016-17 cycle, as mentioned in the executive summary. It is acceptable for auditees to question and challenge the outcome of audits, based on evidence and solid accounting interpretations or legal grounds. We further acknowledge that many of the accounting and legal matters dealt with in the audits are complex and often open to interpretation. But at some auditees, pressure is placed on audit teams to change conclusions purely to avoid negative audit outcomes or the disclosure of irregular expenditure – without sufficient grounds. Often the findings are communicated throughout the audit and even from previous years, but only at end of the audit when outcomes become apparent does the contestation arise.

We experienced such contestation from accounting officers, chief executive officers, boards, chief financial officers and provincial accountants-general and, unfortunately, also from audit committees that should be independent and ensure that management fulfils its responsibilities. Often contestations were escalated to the level of premiers, ministers and members of the executive councils. Contestations included threats of litigation against us and lawyers were increasingly used, at great cost, to contest accounting matters or compliance findings that were not complex or disputable. Our audit processes and the motives of our audit teams were questioned and there were cases of personal threats and intimidation. Delaying tactics were also used whereby information and evidence were not provided as requested.

In our experience, the reason for these contestations was the pressure to improve audit outcomes and performance bonuses often being tied to audit outcomes. Officials and the political leadership also wanted to avoid the consequences and bad press surrounding irregular expenditure. This trend can be reversed if accounting officers and authorities fully and correctly address prior year findings and react to new audit findings and recommendations earlier in the audit process. We also need the National Treasury to play a more proactive role in resolving these disputes. The **leadership should set the tone for accountability** – if audit outcomes are not as desired, energy should be directed to addressing the problem and not to coercing the auditors to change their conclusions.

Please note the following important matters when reading this report:

- We audited 502 public entities in 2016-17. In order to simplify our reporting and ensure that our message is focused on the main entities (422 auditees), we excluded the outcomes of the dormant entities and what we term 'small auditees'. As part of our audit methodology, we classified 163 public entities as small based on the size and nature of their business, and applied a reduced scope of work at these entities. The audit outcomes of these auditees are included in the annexures to this report (which are available on our website), but not in the analysis in this report.
- Every year we increase the number of public entities we audit – most notably in the higher education sector where we systematically increased our auditing of the TVET colleges. In 2016-17, we audited an additional 20 colleges and also performed the audit of the SAA group for the first time. Comparisons year on year are made difficult as the denominator we use in our calculations differs, but we explain the impact of this in appropriate places in the report.
- We refer to the national departments by their full name (e.g. the Department of Basic Education), while we use the shortened version for the provincial departments (e.g. Education).
- We use the following icons in this report to indicate:

A References to the annexures available on our website

Proposed recommendations throughout the report to assist auditees to improve their audit outcomes

Examples to illustrate the effects of weaknesses

Explanations of terminology – we also explain more about our audit process, terminology and abbreviations in section 17

Information on the SOEs audited by private audit firms

When studying the figures, please note that the percentages are calculated based on the completed audits, unless indicated otherwise. Movement over a period is depicted as follows:

Improved

Unchanged Movement of 5% and less: Slightly improved / Slightly regressed

Regressed

NOTES

3 Management and delivery of key programmes

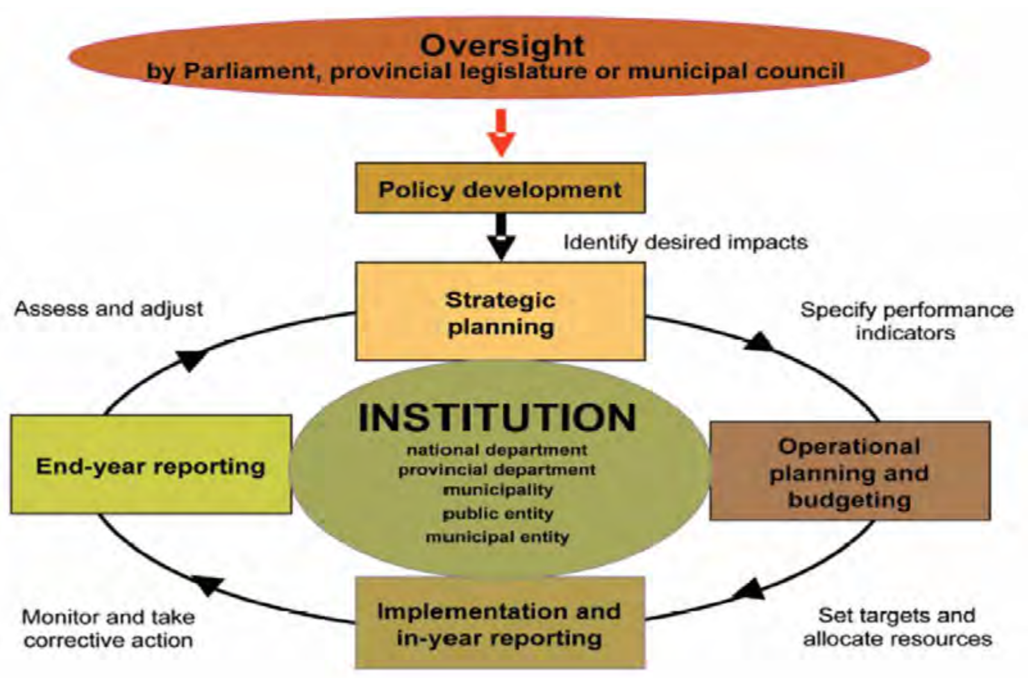
3. *Management and delivery of key programmes*

The NDP launched in 2012 is the long-term strategy for South Africa that focuses on the long-term goals set by government to systemically improve the well-being of the country and its citizens, with the aim of eliminating poverty and reducing inequality by 2030. The sustainable development goals adopted by South Africa drive the same agenda and also aim to protect the planet through sustainable development. **Accountability for government spending: from the plan to the people**, which is a central theme of this report, is about holding the leadership answerable to the public for actions, decisions and policies that should bring about qualitative improvements to the lives of citizens. In addition, it is about determining whether the quality and effectiveness of government spending fall within sustainable financial limits.

The achievement of these goals (**IMPACT**) requires a systematic and well-coordinated process of planning (**PLAN**), disciplined implementation (**DO**), progress monitoring and evaluation (**CHECK**), and corrective action where delivery does not take place as planned (**ACT**).

Against the backdrop of the NDP, the MTSF articulates government's five-year plan to achieve its goals. Through the MTSF, the intended outcomes of the period are determined, which then inform the **strategic plans and budgets of auditees**. The cycle of planning, budgeting and reporting is illustrated below.

Figure 1: Planning, budgeting and reporting cycle



Source: Framework for Managing Programme Performance Information – National Treasury, May 2007

To support the goals set out in the NDP and the MTSF, the 2016-17 budget was tabled in February 2016. This budget was tabled at a time when both global and domestic economic conditions continued to be difficult. Therefore, it is very important for government to exercise sound financial management in the midst of this challenging environment to ensure that government service delivery is not negatively affected.

An abridged version of the budget, called the **estimates of national expenditure** or ENE, was also published. The ENE includes the budget for every national department and what they plan to achieve with the allocated funds. The budget of a department is **broken down into programmes**. Each programme has a specific purpose and objectives that are aligned to the mandate of the department and the objectives of the MTSF. The ENE includes **key performance indicators and targets** that are used to measure whether departments achieved **what they set out to do with the money allocated to them**. A number of the national departments use provincial departments, public entities and other bodies to achieve their objectives and provide funding to them through **grants**. Therefore, the financial information and key performance indicators in the institutional budget plans set out in the ENE provide Parliament and the public with the necessary information to hold government accountable against the outcomes of the MTSF.

Departments also have more detailed annual performance plans that include additional performance indicators and targets, which they then report on through their annual reports. We audit the performance reports and the plans that inform them, by **selecting the most relevant and material programmes and testing whether the indicators and targets are useful and the reported achievements are reliable**. This audit is performed in an **integrated** manner with the audit of the financial statements and compliance with key legislation. At some of the bigger service delivery departments and sectors, we do **additional work on the key projects that enable delivery on these programmes**, often using performance auditors and experts such as engineers to determine if money was used effectively and efficiently – including the quality of project deliverables (e.g. infrastructure projects). This provides us with a unique and comprehensive view of the **management and delivery of key government programmes**. We reported our findings on key programmes to the accounting officers, provincial leadership, ministers and portfolio committees to assist in the accountability and improvement process. In this section, we report on the following five key programmes we had audited, which all have a significant impact on the achievement of government priorities:

- Water infrastructure development
- Expanded public works programme
- School infrastructure
- Food security and agrarian reform
- Housing development finance

We report on the management and delivery of these key programmes to demonstrate the importance of **transparency and accountability for government spending**. Plans and budgets as included in the ENE should translate into service delivery through good financial, performance and project management, supported by the fair and transparent procurement of goods and services. Departments should also report in a credible and transparent manner on how the money was spent and the successes and failures of the funded programmes.

For each programme, we show the following:

- The **budget and purpose** of the programme and how much of the programme **budget had been spent**.
- Whether the key **indicators included in the ENE were achieved** and whether the reported achievement was **reliable**.
- Any **performance planning and reporting concerns** we identified and any **accounting problems** on the programme at the national department.
- **Findings on the key projects** we had audited.
- If a department provided a **grant to provincial departments**, how that grant was **spent and accounted** for by the provincial departments (intergovernmental coordination) and whether the money was **spent in accordance with the grant framework** that defines the intended purpose of the grant. On the projects funded by grants, we indicate whether the **targets were achieved and reliably reported as well as whether we raised any SCM or other findings on the projects**.
- A **conclusion**.

Vote 36 – Department of Water and Sanitation

Programme 3: Water infrastructure development

R12 130 m

R3 841 million of the budget related to the water service infrastructure grant and the regional bulk infrastructure grant.

Programme purpose

Develop, rehabilitate and refurbish raw water resources and water services infrastructure to meet the socio-economic and environmental needs of South Africa.

Key targets planned	*Achievement reported*	*Reliable?*
Number of bulk raw water projects completed during the year = 1	1	√
Number of large water and wastewater services construction projects completed = 3	2	√
Number of mega-water and wastewater services construction projects completed = 1	0	√
Number of small water and wastewater services projects completed per year = 282	31	√

Performance planning and reporting concerns

The department reported on its performance in a reliable and useful manner, but the **programme did not achieve its targets**. The reasons provided by the department for this included the reprioritisation of funds for drought relief and to its trading entity, projects that were behind schedule, and SCM and contracting processes that had been delayed.

The programme is partly enabled through the water service infrastructure grant and the regional bulk infrastructure grant transferred to municipalities. We reported material non-compliance with the Division of Revenue Act by the department, as the **performance of the projects funded by the grants was not evaluated**. The expenditure and non-financial information were also **not monitored in-year**.

Correctly accounted? X	The financial statements of the department did not correctly portray the expenditure, assets, implementing agent arrangements, liabilities and commitments related to this programme. In total, R1,8 billion was shown as a transfer payment even though the affected projects were under the control of the department. The accounting was not in accordance with the Modified Cash Standard and we gave the department a qualified audit opinion as a result.

Concerns regarding water infrastructure projects

We tabled a **stand-alone performance audit** report in November 2016 on water infrastructure, which reported on the planning, management and implementation of water infrastructure projects. Our detailed audit of these projects highlighted weaknesses in the areas of leadership and oversight, funding, project management and intergovernmental coordination. We also reported significant weaknesses in the management of water infrastructure projects at municipalities (funded by the water service infrastructure grant and the regional bulk infrastructure grant) in the **2015-16 general report on local government**.

In 2016-17, we audited 10 key projects administered by the department and implemented by the Water Trading Entity, water boards or a district municipality. We reported the following at an overall level:

- The department enters into contracts with implementing agents (e.g. water boards) to construct capital infrastructure. These **implementing agents need to follow procurement processes and manage contracts in compliance with the same legislation** the department is subject to, as they manage these projects and the funds on the department's behalf. We identified various contraventions of legislation on these projects, which resulted in irregular expenditure. The department could not quantify the irregular expenditure amount in 2016-17. The most common finding was that **competitive bidding processes had not been followed** as the procurement was deemed an emergency, even though it related to multi-year projects. We also reported that the lack of processes and systems at the department to monitor compliance meant that the irregular expenditure could be even more.
- Contractors were overpaid or paid for services not rendered. We could not determine the full extent of the **fruitless and wasteful expenditure** and reported that the department needed to investigate this further.

The projects we audited are listed below, followed by some examples of our findings.

Greater Mbizana regional bulk water supply (EC)	**Lower Thukela** bulk water supply scheme (KZN)	**Giyani** bulk water services and Giyani water services (LP)	**Northern Nsikazi** bulk water scheme (MP)	**Taung / Naledi** (NW)
Mopani emergency project (LP)	**Nwamitwa** dam (LP)	Raising of **Tzaneen dam wall** (LP)	Raising **of Clanwilliam dam wall** (WC)	**Mzimvumbu** water project (EC)

- The Mopani emergency project was not budgeted for in 2016-17 and was not included in the department's annual performance plan, even though the project had been ongoing for a number of years and R98 million was spent in the current year (R364 million to date). The project has now been placed on hold due to a lack of funding.
- The 2016-17 voted budget was overspent on the Lower Thukela and Giyani projects.
- The initial project budgets for five of the nine projects with budgets were insufficient and had to be increased; for example, the budget of the Nwamitwa dam increased from R1,3 billion to R3,7 billion.
- There was non-compliance with SCM legislation on 80% of the projects; for example, the irregular expenditure on the Nwamitwa project was R155,9 million and on the Tzaneen project R43,6 million.
- We assessed the value for money received on some projects and identified the following on the Giyani, Nwamitwa and Tzaneen projects:
  - Double invoices were paid.
  - Professional fees (rates) were not in line with the norm and non-market rates were charged on the actual installation and costs paid.

The programme did not achieve its targets in spite of all the money allocated having been spent. Our audits showed poor planning and project management, inadequate financial management and a serious breakdown in controls. The inadequate monitoring by all role players involved and the lack of accountability and consequences created an environment conducive to service delivery failure and corruption.

Commitments

The portfolio committee committed to increase oversight and monitoring by requesting the department to report quarterly on their audit action plan and status of the project management and control of key infrastructure projects – including those implemented by agents. The committee will also monitor the follow-up of, and actions taken against, those responsible for irregular and fruitless and wasteful expenditure.

Vote 11 – Department of Public Works

Programme 3: Expanded public works programme

R1 953 m

R1 426 million of the budget related to grants to municipalities, provincial departments and non-profit institutions – of which R402 million was the expanded public works programme integrated grant for provinces, which we audited.

Programme purpose

Coordinate the implementation of the expanded public works programme, which aims to create work opportunities and provide training for unskilled, marginalised and unemployed people in South Africa.

Key targets planned	*Achievement reported*	*Reliable?*
Number of public bodies, reporting on expanded public works programme targets, provided with technical support per year = 290	297	X (Should be 190)

Performance planning and reporting concerns

Even though included in the ENE, **the department did not report on the number of work opportunities created** by the programme – the indicator and target were also not included in the 2016-17 annual performance plan. The information was available from the expanded public works programme reporting system, but the department chose not to report thereon as it was unreliable and would have led to material audit findings.

The other key indicator in the ENE on technical support was **incorrectly reported as achieved**.

We further reported to management our concerns regarding the **inadequate reporting by the departments, public entities and municipalities (public bodies) that receive the expanded public works programme grant**. The reports submitted monthly only indicated the amount received and spent, and not the outputs (as required by the grant framework) or how the grant had been utilised.

Concerns regarding the expanded public works programme projects

In 2016-17, we audited 10 expanded public works programme projects across the country, in addition to testing the grants given to the provinces. The projects we audited are listed below, followed by our findings.

Epping and Ndabeni service products (WC)	Recycling, greening and beautification (EC)	Roads and stormwater (**Nkomaba**) (GP)	**Sol Plaatjie** cleaning project (NC)	Maintenance of heritage sites (EC)
VDM borehole operators (LP)	Waste management (MP)	**Escourt** prison (KZN)	Beautification of **DLM** (FS)	**Zeerust** SAPS (NW)

- Work opportunities reported at these projects were not always supported by reliable supporting evidence, such as identity documents, attendance registers and proof of payments.
- Reported beneficiaries were in some cases deceased.
- The identity numbers of some beneficiaries were found to be invalid.
- Some beneficiaries were included on multiple projects when they worked on only one project.

Expanded public works programme integrated grant for provinces

Purpose: To provide incentives to provincial departments to expand work-creation efforts through the use of labour-intensive delivery methods, in compliance with expanded public works programme guidelines. Focus areas include road maintenance, maintenance of buildings as well as tourism and cultural industries.

Results based on 50 projects tested at 41 provincial departments

Budget – R402 million	Spending complied with grant framework?	Correctly accounted for grant in financial statements?
Nine of the 41 provincial departments where we audited the grant underspent by more than 10%. The departments were: • Education (Gauteng) • Health (Free State and Mpumalanga) • Cooperative Governance, Human Settlements and Traditional Affairs (Limpopo) • Social Development (Eastern Cape) • Sport, Arts, Culture and Recreation (Gauteng) • Sport and Recreation (KwaZulu-Natal) • Economic, Small Business Development, Tourism and Environmental Affairs (Free State) • Human Settlements (Mpumalanga)	√	√

Achievement of planned targets for the 50 projects audited

Reliable reporting of achievement?

X

Public Works, Roads and Infrastructure – Limpopo

Supply chain management on projects

None of the 50 projects audited had SCM findings.

Project and grant concerns

The reasons for the underspending on projects varied, and included community unrest, the late appointment or payment of community workers, and delays in finalising service level agreements or project plans.

The department had not put in place adequate internal controls to ensure that reliable information was obtained on the use of the grant money and the number of job opportunities created. As the department did not report transparently on the programme, it could not be determined whether the programme had achieved its targets. The lack of credible information affected the planning and oversight processes and weakened the accountability for this programme.

The national department should enhance the grant agreement signed between the public bodies receiving expanded public works programme funding and the department. This should clarify the evidence that should be maintained, require money received to be reconciled with money spent, and include the number of work opportunities created.

The inclusion of the number of work opportunities created in the annual report of the national department and the enhanced monitoring of the project management and data validation processes of public bodies are essential in improving the overall effectiveness of the programme to achieve the planned six million job opportunities as set out in the MTSF.

Commitments

The public works portfolio committee requested and reviewed a comprehensive action plan prepared by the department to address the root causes that resulted in inaccurate reporting on job opportunities created through the expanded public works programme grant. The action plan included regular site visits by the national department to the public bodies receiving grant funding and the improvement of the expanded public works programme integrated grant template to ensure that proper records which support the reported job opportunities created are consistently maintained. The committee further committed to monitor this plan on a quarterly basis to make certain that it has the desired impact of improving the management and reporting of the expanded public works programme achievements.

Vote 14 – Department of Basic Education

Programme 4: School infrastructure

(Please note that the name of the programme on the ENE is 'planning, information and assessment'.)

R12 621 m

R9 933 million of the budget related to the education infrastructure grant paid to provincial departments of education.

Programme purpose

Promote quality and effective service delivery in the basic education system through planning, implementation and assessment.

Key targets planned	*Achievement reported*	*Reliable?*
Number of new schools built and completed through the accelerated schools infrastructure delivery initiative per year = 59	16	√
Number of schools provided with sanitation facilities through the accelerated schools infrastructure delivery initiative per year = 265	30	√
Number of schools provided with water through the accelerated schools infrastructure delivery initiative per year = 280	29	√
Number of schools provided with electricity through the accelerated schools infrastructure delivery initiative per year = 620	None	√

Performance planning and reporting concerns

The department reported on its performance in a reliable and useful manner, but the **programme did not achieve its targets**. The reasons provided by the department for this included poor performance by contractors and implementing agents, resulting in the termination of contracts, and inferior quality work that had to be redone. Other reasons were weather conditions, a shortage of building material and disruptions due to community unrest. The rationalisation process and mergers of schools on the accelerated schools infrastructure delivery initiative programme further contributed to the set targets not being achieved.

Accelerated schools infrastructure delivery initiative

The department is responsible for the infrastructure development projects funded as part of this initiative. The **objective of the accelerated schools infrastructure delivery initiative** is to eradicate the basic safety norms backlog in schools without water, sanitation and electricity and to replace those schools constructed from inappropriate material such as mud and asbestos to contribute towards levels of optimum learning and teaching.

During the current and previous three years, we reported a number of cases where the completed schools had not been transferred to the custodian department or where it took unnecessarily long to finalise these transfers.

We noted during site visits that classes were **not always used for teaching and learning**. For example, at one of the schools visited, the security guard lived in one of the classrooms and made food inside the room on a paraffin stove. As a result, the floor had been damaged and the walls and cupboards were soiled with food spatter and other foreign matter.

Record keeping for the accelerated schools infrastructure delivery initiative was lacking and resulted in material adjustments to both financial and performance information. The department could not provide credible financial information from implementing agents necessary for the disclosure items in the financial statements of the department, such as commitments, accruals and immovable tangible capital assets. In the case of performance reporting, a significant number of practical completion certificates were obtained from implementing agents only through external audit effort and initiatives of the director-general.

During 2016-17, we conducted infrastructure audits in four provinces, namely the Eastern Cape, Limpopo, Mpumalanga and KwaZulu-Natal. We identified various issues during the audits, which included that adequate project management processes were not in place to manage and monitor the construction schedule and expenditure on the projects. As a result, the following occurred:

- **The services of contractors were terminated** at eight of the 20 projects in the Eastern Cape, which caused delays and increased the cost of projects. One of the reasons given for the terminations was that some contractors cancelled their contract due to financial analysis and undercosting. In some cases, the cost of the replacement contractor was more than the original contract. Also, in most cases the **total cost of the project was more than the original value**.
- **Delays** of between four and 14 months were experienced on all projects in Mpumalanga. Delays of between three and 22 months were experienced on all projects in the Eastern Cape. Some of the reasons given for these delays were additional work having to be carried out on site, scope changes as well as an inability to obtain materials.
- The department did not submit all information requested for audit purposes. A **limitation of scope** was experienced in all four provinces, with the majority of the outstanding information being in KwaZulu-Natal and Limpopo.
- No progress had been made on two projects in KwaZulu-Natal that had been **dormant since the previous audit in 2016**, and the contractors had abandoned the projects. In addition, we noted quality issues during site visits to both of these projects.
- Quality issues were also noted in the other three provinces, as illustrated in the pictures below.

The Enviro Loo vent pipes were not stable and the pipes could be moved easily by hand (Limpopo)

Damaged bricks used to build walls (Phutlo Secondary School, Limpopo)

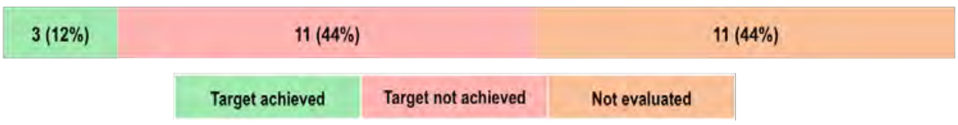
Education infrastructure grant

Purpose: Help accelerate the construction, maintenance, upgrading and rehabilitation of new and existing infrastructure in education, including district and circuit accommodation; enhance capacity to deliver infrastructure in education; address damage to infrastructure caused by natural disasters; and address the achievement of the targets set out in the minimum norms and standards for school infrastructure.

Results based on 25 projects tested at the nine provincial departments

Budget – R9 933 million	Spending complied with grant framework?	Correctly accounted for grant in financial statements?
Two of the nine departments where we audited the grant underspent by more than 10%.	X Free State	X Free State and Mpumalanga

Achievement of planned targets for the 25 projects audited

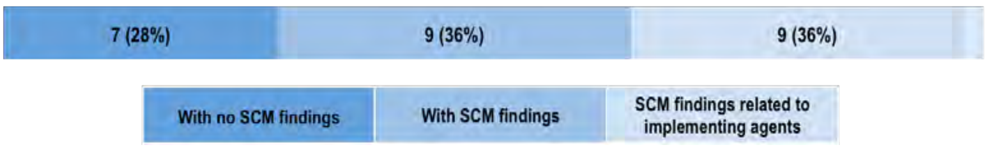


Reliable reporting of achievement?

X

KwaZulu-Natal and Limpopo

Supply chain management on projects



Project and grant concerns

The Free State **underspent their budget by more than 10%** as investigations resulted in some projects being delayed. In Mpumalanga, the underspending was as a result of delays in appointing contractors.

Planned targets **were not achieved or not even evaluated on 88%** of the projects. In addition, the reported achievements were **not reliable in two provinces**.

Money was used in accordance with the grant framework except in the Free State. However, the prevalence of SCM findings on most of the projects raised questions about the **appropriateness of the spending** – especially where implementing agents were used.

The following are some of the findings we reported on the projects:

- Some departments **did not have enough capacity** to implement projects and relied heavily on consultants and project managers.
- The lack of consequences for poor performance and transgressions resulted in **shortcomings previously reported being repeated** and action plans developed not being adequately implemented.
- The provincial departments and their implementing agents did not effectively plan and manage projects. This resulted in the following:
  - We noted **poor quality work and poor workmanship** in six provinces. Furthermore, in four provinces, the assessment and certification of work performed were not well managed, which resulted in payments for substandard or poor quality work.
  - There were **delays in the completion of projects in eight provinces**. In three provinces, the delays were due to the late payment of the contractors by the departments and/or their implementing agents.
  - The **Standard for Infrastructure Procurement and Delivery Management** was not fully implemented in certain provinces.
  - There were a high number of **variation orders** in four provinces (Free State, Gauteng, KwaZulu-Natal and Northern Cape). These variation orders were approved for items that should have been included in the scope, which resulted in increased contract values.

The programme missed its targets by a significant margin. Poor planning and project management, inadequate and non-compliant procurement and contract management practices, and a lack of credible reporting hampered successful delivery on this very important initiative. The lack of accountability and consequences sustained an environment in which poor performance and irregularities were seen as business as usual.

Commitments

Action plans will be developed by all heads of departments within the education sector by 31 October 2017 to address the weaknesses and deficiencies identified in the internal control environment at the provincial departments and to ensure that the deficiencies identified in previous years have been adequately addressed.

The education sector will focus on improving **coordination** between various departments (within and outside the education sector) and key role players such as implementing agents and contractors to enhance accountability and improve understanding between various stakeholders of their roles and responsibilities in achieving sector objectives. This should have a positive impact on service delivery.

Monitoring and evaluation processes will be strenghened to ensure frequent monitoring by dedicated staff of the various infrastructure projects in progress across all phases of construction to detect and prevent the risks that delay and impede service delivery.

Consequence management will be intensified to ensure that officials are held accountable and to minimise transgressions.

Vote 24 – Department of Agriculture, Forestry and Fisheries

Programme 3: Food security and agrarian reform

R1 881 m

R1 642 million of the budget related to the comprehensive agricultural support programme grant paid to provincial departments of agriculture.

Programme purpose

Facilitate and promote food security and agrarian reform programmes and initiatives.

Key targets planned	*Achievement reported*	*Reliable?*
Number of smallholder producers supported per year = 16 000	17 004	√
Number of hectares in underutilised areas cultivated in communal areas per year = 120 000	35 213 (Affected by drought)	√

Performance planning and reporting concerns

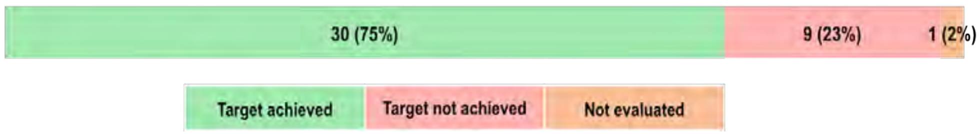
We reported material non-compliance with the Division of Revenue Act, as the department **did not adequately monitor the expenditure and non-financial performance information** on the projects funded by the grants that support this programme.

Comprehensive agricultural support programme grant

Purpose: Provide effective agricultural support services; promote and facilitate agricultural development by targeting beneficiaries of land reform, restitution and redistribution, and other black producers who have acquired land through private means and are engaged in value-adding enterprises domestically or involved in export; and address damage to infrastructure caused by floods.

Results based on 40 projects tested at the eight provincial departments

Budget – R1 642 million	**Spending complied with grant framework?**	**Correctly accounted for grant in financial statements?**
None of the departments where we audited the grant underspent by more than 10%.	X Free State and KwaZulu-Natal	X Free State, North West, Gauteng and KwaZulu-Natal

Achievement of planned targets for the 40 projects audited	Reliable reporting of achievement?
	X Free State

Supply chain management on projects

Project and grant concerns

The grant was spent by the provincial departments **but targets were not always achieved or assessed**.

The grant was not spent in accordance with the grant framework in two provinces – the national department did not identify this as a result of poor monitoring practices.

Just over 40% of the projects funded by this grant that we had audited were plagued by **SCM irregularities, with a fifth of these irregularities being on projects where implementing agents were used**. The non-compliance typically related to the appointment of the implementing agent or the agent following inadequate procurement processes.

The incorrect accounting related to the **grant received and paid over to the implementing agent being shown as transfer payments** by the departments, which is contrary to the requirements of the Modified Cash Standard. It also resulted in a loss of accountability by some departments of the money spent and the ownership of the assets developed or purchased. Two departments in this sector received a qualified audit opinion as a result of incorrect reporting.

It is not possible to determine whether the programme achieved its targets as a result of inadequate and unreliable reporting on the programme and the projects supported by the grant. The departments had not put adequate internal controls in place to ensure that reliable information was obtained on the use of the grant money and the achievement of targets. We have serious concerns regarding the projects implemented in the provinces and whether the money was used for its intended purposes, especially where implementing agents were used and the provincial departments did not take accountability for the projects – whether in their financial statements or through monitoring and oversight.

Commitments

The department committed to prioritise its resources to create capacity to monitor the performance of the programme's initiatives and deliverables. The portfolio committee also committed to support the department to enhance its capacity to effectively monitor the performance of this programme. The committee further agreed with the department's view that the inadequate monitoring of the programme's performance was a consequence of underfunding of the operations of the department where available resources had to be prioritised for more urgent and critical activities.

Vote 38 – Department of Human Settlements

Programme 4: Housing development finance

R29 931 m

R29 124 million of the budget related to grants to municipalities and provincial departments – of which R18 284 million was the human settlements development grant for provinces, which we audited.

Programme purpose

Fund the delivery of housing and human settlements programmes and manage all matters related to improving access to housing finance and developing partnerships with the financial sector.

Key targets planned	*Achievement reported*	*Reliable?*
Number of subsidy housing opportunities provided = 115 000	90 692	√
Number of affordable rental opportunities delivered = 3 700	5 040	√
Number of households upgraded to phase 2 = 175 000	75 941	√
Number of catalytic projects implemented = 15	15	√
Number of finance-linked individual subsidy programme subsidies allocated to approved beneficiaries per year = 17 231	2 660	√

Performance planning and reporting concerns

The department reported on its performance in a reliable and useful manner, but the **programme did not achieve some of its key targets**. The reasons provided by the department for this included project delays (also because of weather conditions) and delays in council approval for upgrades. The reasons for the underachievement on the subsidy programme were the sluggish economy and over-indebtedness of customers.

Human settlements development grant

Purpose: Provide funding for the creation of sustainable and integrated human settlements.

Results based on 84 projects tested at the nine provincial departments		
Budget – R18 284 million None of the departments where we audited the grant underspent by more than 10%.	**Spending complied with grant framework?** √	**Correctly accounted for grant in financial statements?** √

Achievement of planned targets for the 84 projects audited

Reliable reporting of achievement?

√

Supply chain management on projects

Project and grant concerns

The following provinces did not meet the delivery of their targets by more than 70%:

- Free State (only 38% of planned sites were serviced)
- Gauteng (only 59% of planned houses were built)
- Mpumalanga (only 42% of planned houses were built)

We identified non-compliance with SCM legislation on 45% of the projects we audited, mostly on projects where implementing agents were used.

We raised SCM findings relating to the appointment of service providers for the construction of houses, which resulted in irregular expenditure, in the following provinces:

- Free State – irregular expenditure of R974 million
- Mpumalanga – irregular expenditure of R745 million
- KwaZulu-Natal – irregular expenditure of R559 million
- Gauteng – irregular expenditure of R345,5 million

Furthermore, we raised the following findings during the audit of Princess Plots (Phase 1: Show Village) and Lawley Extension 3 & 4 in Gauteng, and Naledi Vryburg, Naledi Huhudi and Mamusa Glaudina in North West:

- Delays of between 18 and 20 months were experienced on the Princess Plots and Naledi Vryburg projects. This was due to the late approval by municipalities of construction drawings. In addition, adequate project management processes were not in place to prevent project delays. At Princess Plots, the delays led to community protests.
- Overspending of R20 956 478 was noted on the Princess Plots project, while fruitless and wasteful expenditure of R87 936 656 was incurred on 503 housing units that were constructed and demolished as part of the Naledi Vryburg project.
- The provincial human settlements departments in Gauteng and North West had lists of projects that had to be implemented. The projects were not prioritised, however, as the departments viewed all projects as equally important, which resulted in the milestones of some projects not being met.
- We identified quality defects such as cracks in floors and walls, inconsistent mortar application and incorrectly constructed or sealed joints on projects such as the Naledi Huhudi project, as illustrated on the following page. Certain quality defects were due to poor workmanship by the contractor and a lack of supervision of the contractor by the implementing agent and/or the provincial department. Such defects will reduce the lifespan of the infrastructure.


Staircase crack above window, indicating a lack of a lintel or poorly reinforced brickwork


Cracks and honeycombing on external apron, indicating poor construction and concrete mix

The department should pay close attention to compliance with procurement and SCM requirements to avoid irregular expenditure. Furthermore, contract and project management should be enhanced in the Eastern Cape, Gauteng, KwaZulu-Natal, Mpumalanga and North West, as poor planning, insufficient controls and inadequate project monitoring threaten the success of this programme. The department should also enhance the monitoring of grant expenditure to ensure that grant funding is spent on its intended purpose and in accordance with applicable laws and regulations. This will further ensure that planned targets are achieved through tracking expenditure against the budget and deliverables.

Commitments

The director-general committed to initiate a process of implementing customised indicators for the human settlements development grant received by the provincial departments to ensure consistent reporting and the achievement of the planned deliverable of 563 000 houses over the MTSF period, and to further strengthen the national department's ability to monitor spending of this grant.

Conclusion

Only 22% of the targets highlighted in the ENE were achieved – even though 98% of the allocated budgets had been spent. Where grants were given to provincial departments, the spending and achievement of targets were not adequately monitored on most of the programmes. In some cases, the provincial departments did not report on the performance of the projects funded by the programme or did not report reliably.

Accounting for the expenditure, liabilities and assets related to the programmes was not always credible and resulted in qualifications in the financial statements of departments, especially where the departments used implementing agents to manage projects. Irregularities in procurement processes and inadequate contract management were common on the projects. Some of the projects funded through these programmes displayed serious weaknesses in terms of delayed delivery, poor quality work, waste and mismanagement.

The following were the main reasons for the inadequate performance on these programmes at the national departments and the provincial departments that received the grants:

Poor planning (including budgeting and setting realistic targets) (**PLAN**).

Financial and performance management and project management that did not provide for the disciplined and controlled implementation of projects and the credible monitoring and reporting of financial and non-financial information (**DO**).

Inadequate monitoring of projects and grants (**CHECK**).

Lack of corrective actions to address project failures and SCM irregularities (**ACT**).

We intend to increase our focus in the audits of these key programmes – specifically on how the money is being spent without achieving the intended targets.

4 Status of state-owned enterprises

4. *Status of state-owned enterprises*

The public entities defined in the Public Finance Management Act (PFMA) include government business enterprises, more commonly known as state-owned enterprises or SOEs. In this section, we specifically **focus on the status of major public entities**, as listed in schedule 2 of the PFMA. These SOEs are independent entities partially or fully owned by the state to achieve the various socio-economic goals of government – they are expected to fulfil a dual commercial and developmental mandate.

Most of these SOEs have a **direct impact on the lives of citizens** through the services and infrastructure they provide. Poor governance, mismanagement, fraud and corruption claims and a lack of financial sustainability at some of the SOEs have been in the spotlight for the past few years – attracting attention as taxpayers' money is used to sustain the failing SOEs. As this narrative contributes to the loss of public confidence in the ability of the state to govern and oversee these SOEs, we have included our findings on the state of SOEs in this report based on our audits.

We **do not audit all the SOEs** – some are audited by private audit firms in accordance with the directives we provide using our methodology for auditing compliance and performance information. These audit firms are appointed by the boards of the SOEs. We maintain a close relationship with the appointed audit firms, in particular with those auditing SOEs we categorised as **significant-risk entities**. It allows us to continuously increase our oversight and involvement in these audits in order to improve consistency in auditing and reporting on all SOEs and to provide guidance and support on technical and governance matters. We can opt to perform these audits and we have significantly increased the number of SOEs we audit over the past few years.

Table 1 shows which audits we performed in 2016-17 and on which we report in this section. It also shows those audited by audit firms and which have been identified as significant-risk entities for increased oversight by the Auditor-General of South Africa (AGSA). Their audit outcomes are not included in the analysis in this section but we include some observations in this regard. The subsidiaries that are classified as small auditees are not included in the table below or in our analysis.

The **budgets** administered by the 25 SOEs (including the subsidiaries) we audit totalled R31 billion in 2016-17 – 17% of the total public entity budget and 3% of the total 2016-17 budget of departments and public entities.

Table 1: Audit of state-owned enterprises

SOEs audited by the AGSA	SOEs audited by audit firms
Independent Development Trust	Telkom SA *and its subsidiaries*
Acsa	Trans-Caledon Tunnel Authority
Sapo *and its subsidiary Courier and Freight Group*	Industrial Development Corporation of South Africa
Land Bank *and its subsidiaries Land Bank Life Insurance and Land Bank Insurance*	Alexkor
Armscor	Broadband Infraco
SABC	Development Bank of Southern Africa
Central Energy Fund *and its subsidiaries PetroSA, PetroSA Ghana, SA Agency for Promotion of Petroleum Exploration and Exploitation (Petroleum Agency SA), and Strategic Fuel Fund*	Air Traffic and Navigation Service Company
Necsa *and its subsidiaries Gammatec NDT Supplies, NTP Radioisotopes and Pelchem*	**Significant-risk SOEs audited by audit firms**
SA Express	Denel *and its subsidiaries*
South African Forest Company (Safcol) *and its subsidiary Komatiland Forests*	Transnet *and its subsidiaries*
SAA *and its subsidiaries Air Chefs, Mango Airlines and SAA Technical*	Eskom *and its subsidiaries*

Overall audit outcomes

We set the cut-off date for inclusion of the audit outcomes in this report as 31 August 2017. By this date, the following six **audits had not been completed**:

- **SAA and subsidiaries** (four SOEs) – this is the first year that we have audited the SAA group. Except for Mango Airlines, we have not yet received the final financial statements of the group. The four companies in the SAA group received clean audits in the previous year.
- **SA Express** again submitted their financial statements late (only by 31 August). This company received a qualified audit opinion last year with material findings on their performance reporting and compliance with legislation.
- The **Independent Development Trust** received a qualified audit opinion in 2013-14 and subsequently received disclaimed opinions in the 2014-15 and 2015-16 financial years after deficiencies were identified in management's processes to appropriately account for programme expenditure. The delay in submitting information had an overall negative impact on the timely finalisation of the 2016-17 audit. The audit was subsequently completed but was too late to be included in the analysis in this report. The entity again received a disclaimed opinion as information was not available to support the occurrence of programme expenditure in the financial year it related to with material findings on performance reporting and compliance with SCM legislation. However, the entity had made progress in some areas since the previous year.

Figure 1 reflects the audit outcomes of the 19 completed audits over four years.

Figure 1: Audit outcomes over four years

The **audit outcomes regressed** over the four-year period and from the previous year – the outcomes are likely to be even worse once the outstanding audit results are included.

The SOEs with **clean audit outcomes** were Armscor (for the past three years), Land Bank Life Insurance (for the past three years) and three SOE subsidiaries that had improved to a clean audit status (Gammatec NDT Supplies, NTP Radioisotopes and PetroSA Ghana). Petroleum Agency SA and Land Bank Insurance lost their clean audit status of the previous year as a result of material non-compliance with legislation.

The audit outcomes of the **SOEs audited by private audit firms** (which are not included in the graphic above) **also regressed** from the previous year. The following three regressed:

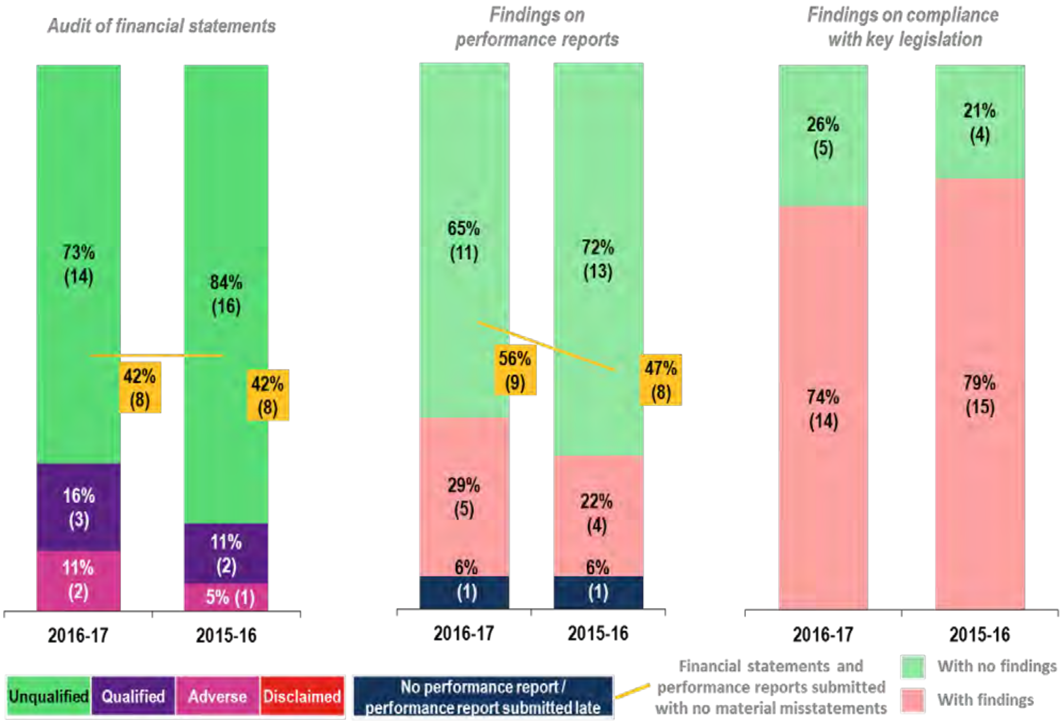
- Broadband Infraco lost its clean audit status as a result of material findings on compliance and their performance report, while Air Traffic Navigate Services did so as a result of various material misstatements in their financial statements and material findings on compliance with legislation.
- Eskom was qualified as all irregular expenditure incurred was not disclosed and due to material findings on compliance with SCM legislation.

The audit opinion of Transnet remained unchanged as unqualified with findings on performance reporting and compliance.

The audit opinion of Denel had not yet been finalised at the date of this report.

Figure 2 shows the audit opinions on the financial statements and the findings on the performance reports over two years as well as the percentage of SOEs that submitted financial statements and performance reports without material misstatements (orange line). It also shows the number of SOEs that had material findings on compliance with key legislation in the past two years.

Figure 2: Audit outcomes on three key areas



As shown in figure 2, the SOEs regressed in all areas except for compliance with legislation in which there was a slight improvement. The **regression in the quality of the financial statements** was as a result of the following:

- The SABC regressed from a qualified opinion to an adverse opinion and the Courier and Freight Group (a subsidiary of Sapo) retained its previous year's adverse opinion – both had various material misstatements in their financial statements and could not substantiate that they are going concerns (going concern is discussed later on in this section).
- Sapo remained qualified in areas such as property, plant and equipment as well as irregular expenditure.
- Safcol and its subsidiary Komatiland Forests regressed to a qualified opinion, as they did not disclose all the irregular expenditure incurred.

Although 14 SOEs had unqualified audit opinions, only eight submitted financial statements without material misstatements. This means that six SOEs, which include Acsa, Necsa and most of the Central Energy Fund group, received an **unqualified opinion only because they corrected all the misstatements we had identified in the audit**.

We highlight the following with regard to the **performance reports** of the SOEs:

- The Courier and Freight Group again did not prepare a report on its performance as required by the PFMA.
- Some of the indicators and targets reported on by the SABC and Sapo were not useful, as there was no clear and logical link between the indicator and the strategic objective to which it related (SABC) or the source of information and method of calculation and/or the target set was not clearly defined (Sapo). Both these SOEs also did not report in a reliable manner, as some of the achievements were misstated or we could not find evidence that substantiated the achievements.
- Safcol, Acsa and PetroSA also did not report reliably – but only on a few targets.

The indicators and targets in the performance reports form an important tool for shareholder departments and ministers to keep SOEs accountable against set outcomes and goals. Weaknesses in the performance reports therefore need to be addressed to ensure that the direction and oversight provided by the shareholders are clear and focus on the things that matter.

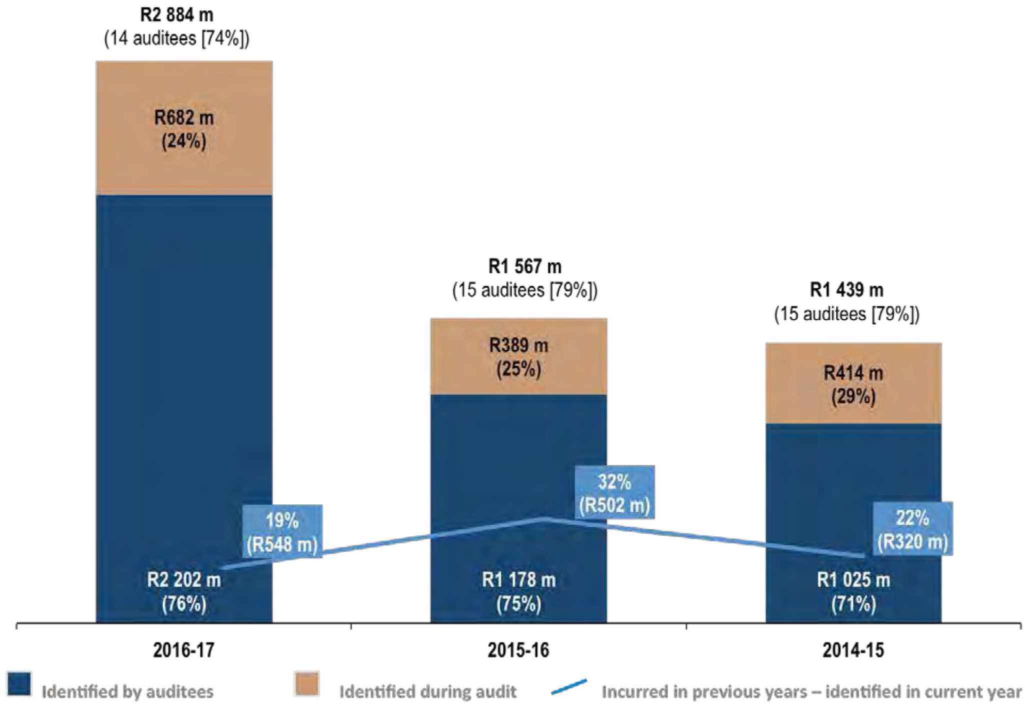
The **slight improvement in compliance with legislation** was as a result of three SOEs addressing their previous year's findings, but two regressing in this area.

The internal controls that should ensure the quality of financial statements and performance reports as well as compliance with legislation were not in place at all SOEs, resulting in these outcomes.
The weakest control areas were their policies and procedures, IT system controls, and compliance monitoring. A discipline of regular in-year reporting and monitoring of financial and non-financial results had also not been established.

Irregular expenditure and supply chain management

Figure 3 shows the **three-year trend in irregular expenditure** based on the amounts that were disclosed in the financial statements of the SOEs. It also indicates the percentage of irregular expenditure identified by them versus that identified by the audit process as well as the proportion of irregular expenditure disclosed that had been incurred in previous years but only identified in the current year (blue line).

Figure 3: Irregular expenditure over three years



The number of SOEs with irregular expenditure decreased slightly but the **value increased significantly**. The main contributors were the following:

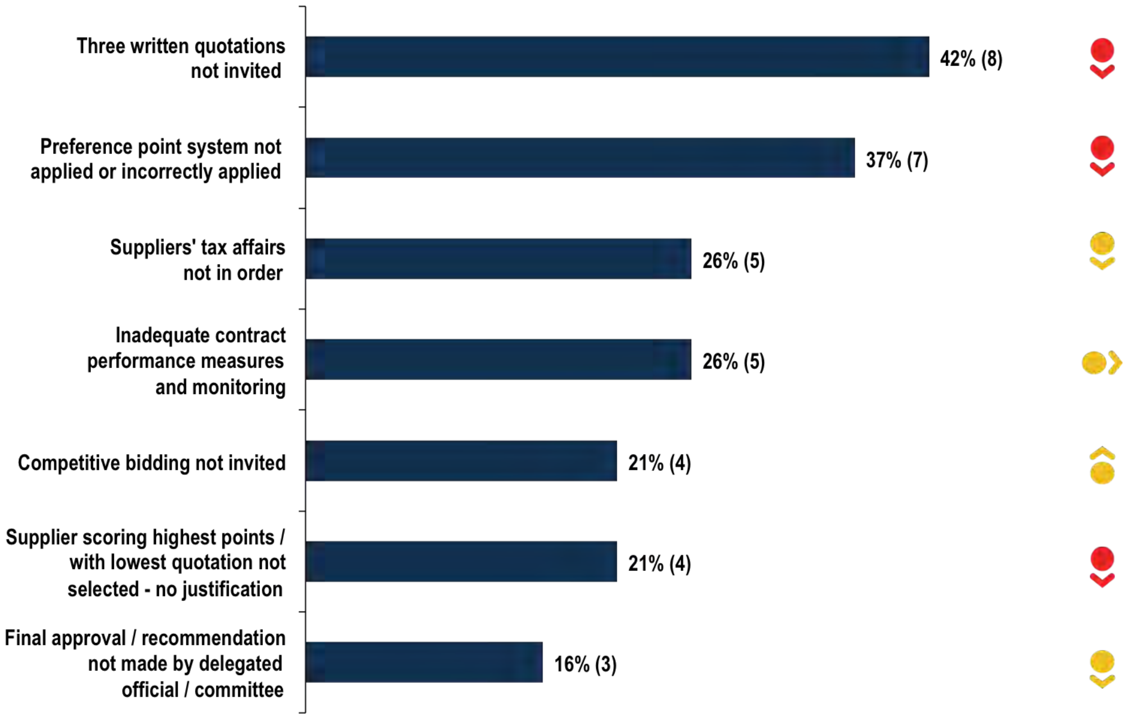
- Acsa – R1 169 million (2015-16: R134 million) – 60% was as a result of non-compliance with legislation on contracts.
- Sapo – R719 million (2015-16: R127 million) – 45% was as result of non-compliance with procurement process requirements and 37% as a result of not following competitive bidding or quotation processes.
- SABC – R687 million (2015-16: R764 million) – 75% was a result of not following competitive bidding or quotation processes.
- Komatiland Forests – R238 million (2015-16: R37 million) – 49% was a result of not following competitive bidding or quotation processes.

The irregular expenditure of the significant-risk SOEs we do not audit was:

- Eskom – R4 043 million
- Transnet – R923 million
- Denel – R146 million

Figure 4 shows the most common SCM findings at SOEs with an indication of the movement from the previous year.

Figure 4: Most common supply chain management findings



As shown in figure 4, the number of **SOEs with findings had increased** from 2015-16 in most areas.

The PFMA requires SOEs to put policies and processes in place to ensure that their procurement processes are fair, equitable, transparent and competitive. Although SCM policies were in place, we found that officials were not familiar with the policies and the procurement processes they should follow, and in some cases circumvented the processes. We could also not always find evidence for the decisions made to award contracts to certain suppliers.

Financial sustainability

Schedule 2 public entities are business enterprises that are required to generate revenue to fund their operations. However, some are dependent on government support in the form of government guarantees or subsidies. The state as owner has committed to ensuring that SOEs have adequate funding to operate and achieve their developmental and commercial objectives. The well-publicised financial woes of SOEs such as SAA, Sapo and the SABC put a spotlight on the financial sustainability of SOEs and the impact of their failures on dwindling state resources.

Our audits focused on some key aspects of the financial health of SOEs – in particular the assessment of going concern.

What is going concern?

The accounting standards require that when financial statements are prepared, management must assess the entity's ability to continue as a going concern. This means that they have to assess whether they will be able to continue their operations for at least another 12 months and will not go out of business and liquidate their assets.

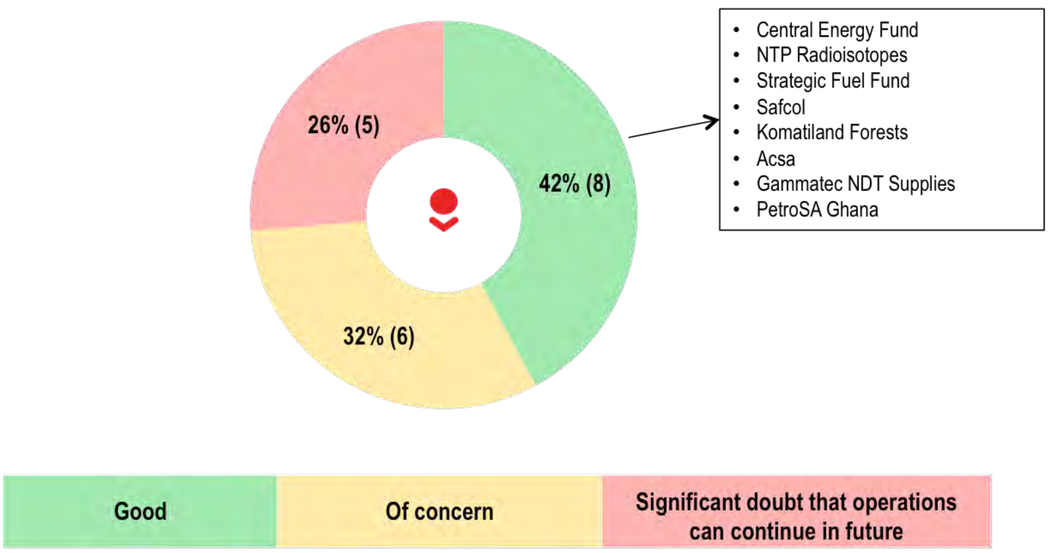
If they determine that the entity does not have the capacity or prospect to raise enough financial resources to stay operational, the financial statements need to be prepared as if they are going out of business.

If this assessment confirms that the entity is a going concern but identifies that there is a material uncertainty about their ability to continue as a going concern in future, this must be disclosed in the financial statements.

Our role as auditors is to audit management's assessment and obtain evidence about the appropriateness thereof.

Our assessment of the financial health of SOEs is shown in figure 5.

Figure 5: Status of financial health



The **financial health of SOEs had regressed from the previous year**. For just over a quarter of them there was significant doubt on whether they could continue their operations in future, as outlined below:

- The **SABC was commercially insolvent** by the end of the financial year. They incurred a net deficit (loss) for the past two years and we are of the opinion that they will not be able to pay their debt when it becomes due. Subsequent to year-end, they applied for a government guarantee to enable them to borrow money to settle their obligations. The SABC did not disclose these material financial uncertainties and we could not conclude on the viability of the SABC without a guarantee. As a result, their financial statements received an adverse opinion.
- **The Courier and Freight Group** is a subsidiary of Sapo, which made a substantial loss in 2016-17 and 2015-16 with their liabilities far exceeding their assets. As no arrangements were approved for Sapo to give financial assistance to their subsidiary, we deemed this company to **not be a going concern** and gave them an adverse opinion as their financial statements did not reflect this.
- **Sapo** itself disclosed that conditions existed (including a loss of R978 million) that were indicative of a **material uncertainty whether the company and the group could continue as a going concern.**

- **PetroSA and Pelchem** disclosed that they might also not be able to continue as a going concern in future based on the significant losses by these companies.

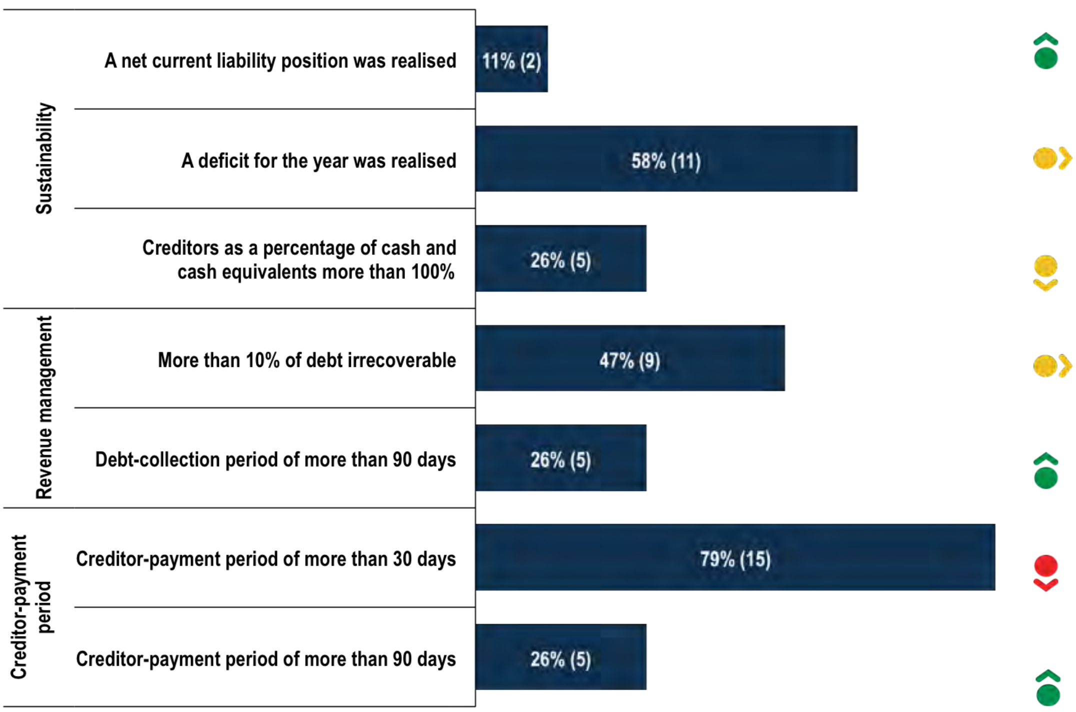
SAA and all its subsidiaries (except Mango Airlines) **had not submitted their financial statements** for auditing by the time of this report, as management could not conclude on whether these companies were going concerns.

We are also concerned that the **losses incurred in 2016-17** by **Armscor, Necsa, Land Bank Insurance and Petroleum Agency SA** could be an indication of a possible going concern problem at these entities in future. We also identified some concerning indicators at **Land Bank** itself and its other subsidiary **Land Bank Life Insurance**.

These SOEs have put forward various reasons for them recording less than favourable financial results in recent times. These include the downturn in the economic markets with most of these SOEs heavily exposed to the international markets; increased commodity prices that directly affect the SOEs due to their role as infrastructure providers to the South African economy; and weak commercial and financial decision-making where SOEs are trapped in onerous contracts. In our view, leadership instability, poor decision-making and inadequate financial management controls and processes also contributed to the poor financial state of SOEs.

Figure 6 provides an overview of the status of key financial indicators at the SOEs we audited and the movement from the previous year.

Figure 6: Financial health indicators



The government departments responsible for the SOEs issued guarantees with the approval of the minister of Finance for them to obtain funding from lenders and other external parties. These guarantees are issued in terms of the PFMA.

What is a guarantee?

'Guarantee' is a legal term more comprehensive and of higher importance than either warranty or security.

By granting a guarantee, the state is therefore providing surety to a lender that the state will repay amounts due to the lender in terms of the agreement if the SOE is not in a position to do so.

A guarantee is typically in the form of a letter confirming the conditions of the guarantee addressed to the SOE and signed by the minister of Finance.

A lender will typically be either a local or foreign bank.

These guarantees can be a direct charge to the **National Revenue Fund** should the SOEs default on their guaranteed liabilities. The fund keeps record of guarantees issued and the total exposure to the government. The audit of the National Revenue Fund will only be finalised after the date of this report, but based on the audit work already done, guarantees had been issued to 12 SOEs (including the SOEs not audited by us) to an amount of R440,26 billion and government had exposure to a total liability of R243 billion. Of the total guarantees, R350 billion was issued to Eskom, with a R203 billion exposure.

The amount stated as total exposure means that the SOEs utilised the guarantee to obtain loans from lenders. We also raised findings during the current year's audit on the incomplete and inaccurate recording of the guarantees and exposure.

We will continue to increase our audit focus on the ability of the state to back up these guarantees with funds if called upon to pay SOE creditors – as has been done for SAA.

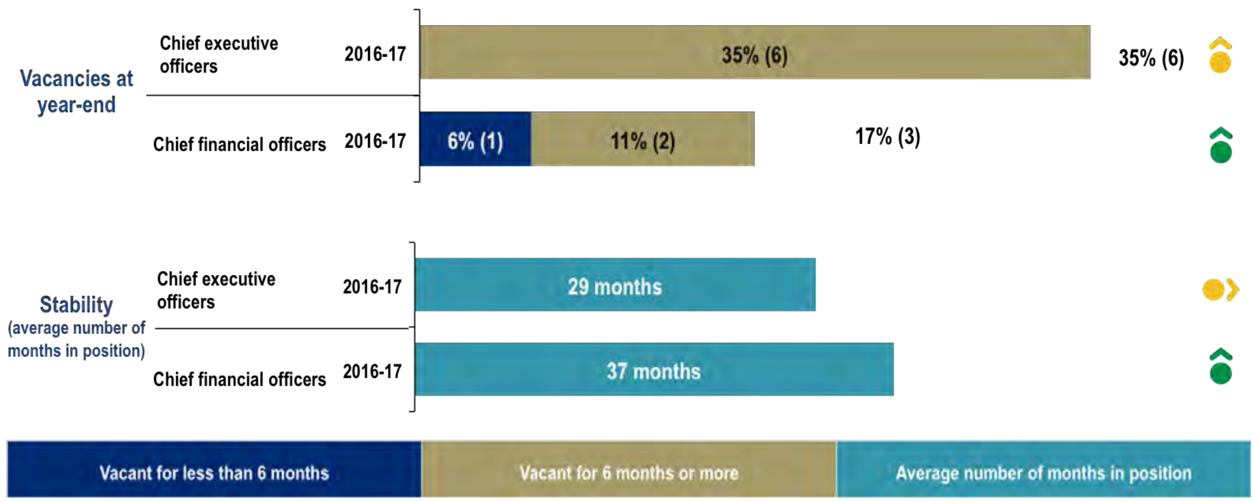
Most of the SOEs we audit are state-owned companies that are subject to the Companies Act. The act prohibits companies from carrying on its business recklessly or with gross negligence, and determines that directors can be held personally liable for any losses suffered as a result of such reckless trading.
As more and more state-owned companies cannot pay their debts as they become due, and government does not always provide the financial support requested (e.g. at the SABC and the Courier and Freight Group), directors are being placed in very difficult situations when they need to make business decisions or enter into contracts. Delays by government in making policy decisions on state-owned companies and how they will be financially supported further **worsen the outlook of state-owned companies in the short and medium term.**

Leadership instability and oversight

As part of our audits, we considered the leadership, financial and performance management as well as governance of auditees to identify the possible root causes of poor audit outcomes, irregular expenditure and financial health concerns.

Instability at board and executive levels played a role in the outcomes of SOEs. At the SABC, for example, the board did not quorate for most of the financial year and the interim board was put in place only at the end of the financial year. Figure 7 shows the extent of vacancies at year-end in the chief executive officer and chief financial officer positions as well as the period that the positions had been vacant. It further shows the average number of months the current incumbents had been in their positions.

Figure 7: Vacancies and stability



Six of the SOEs **did not have chief executive officers at year-end** – a slight improvement from the previous year. The chief executive officers at the other SOEs had only been in those positions for an average of nearly 2,5 years. The vacancy rate and stability in chief financial officer positions were less concerning and continued to improve.

Vacancies at senior management level further contributed to the weaknesses identified – the average vacancy rate was 17%, with both SOEs in the Safcol group at a 60% vacancy level. Generally, the **quality of the finance units** was acceptable (at 79%) – staff vacancies did have an impact at Acsa, while both vacancies and skills were a concern in the Sapo group.

An emerging risk is a lack of **appropriate skills at board level –** the bad reputation of some of the SOEs can also contribute to them not attracting the right level of skills and experience.

The **level of oversight by the departments** the SOEs report to differed and there was no single approach in this regard. The political leadership was also inconsistent – at some SOEs there was a high level of involvement, while at others the required decision-making and policy direction were not provided timeously (e.g. board appointments).

Conclusion

SOEs play an important role in South Africa: they need to be supported by the state but also called to account. Government should work towards a **consistent strategy** for SOEs, which includes firm commitments to support strategic SOEs where the economic climate is affecting their sustainability (**PLAN**). SOEs should **strengthen their financial and performance management systems** to account in a credible manner on their finances and performance (**DO**). The **oversight** by the departments, ministers and parliamentary committees responsible for the SOEs should include strong in-year monitoring and ensuring that governance policies and practices are in place (**CHECK**). Boards and chief executive officers should be **held accountable** for the delivery and financial results of the SOEs, and there must be immediate and effective consequences for poor performance and transgressions (**ACT**).

NOTES

5 Financial health and unauthorised expenditure

5. Financial health and unauthorised expenditure

The accountability for government spending includes taking **accountability for the financial health** of auditees. The current economic climate increases the pressure on auditees to make sound financial decisions and contain costs. The need for service delivery continues to increase but budgets are being cut and other revenue streams are under strain. This section provides our view of financial health based on an analysis of the financial statements and the unauthorised expenditure incurred by departments.

Our audits included a high-level analysis of **10 financial health indicators for departments** and **nine financial health indicators for public entities** to provide management with an overview of selected aspects of their current financial management and to enable timely remedial action where the auditees' operations and service delivery may be at risk. We also performed audit procedures to assess whether there were any events or conditions that might cast significant doubt on an auditee's ability to continue its operations in the near future. Based on the analysis, each auditee was given an overall assessment as follows:

Good	Two or fewer unfavourable indicators
Of concern	More than two unfavourable indicators
Intervention required	Significant doubt that operations can continue in future and/or where auditees received a disclaimed or adverse opinion, which meant that the financial statements were not reliable enough for analysis

Figure 1 shows our assessment of the **financial health of auditees over the past four years** and figure 2 the **status in provinces and the national sphere** with a comparison to the previous year.
The 2015-16 figures have been restated to take into account changes in the indicators used to assess the financial health of auditees. Note also that these two figures include the financial health status of the SOEs to provide an overall picture, but the SOEs are not included in the discussion on the status of public entities as they had already been dealt with in section 4.

Figure 1: Number of auditees with indicators of financial health risks (overall)

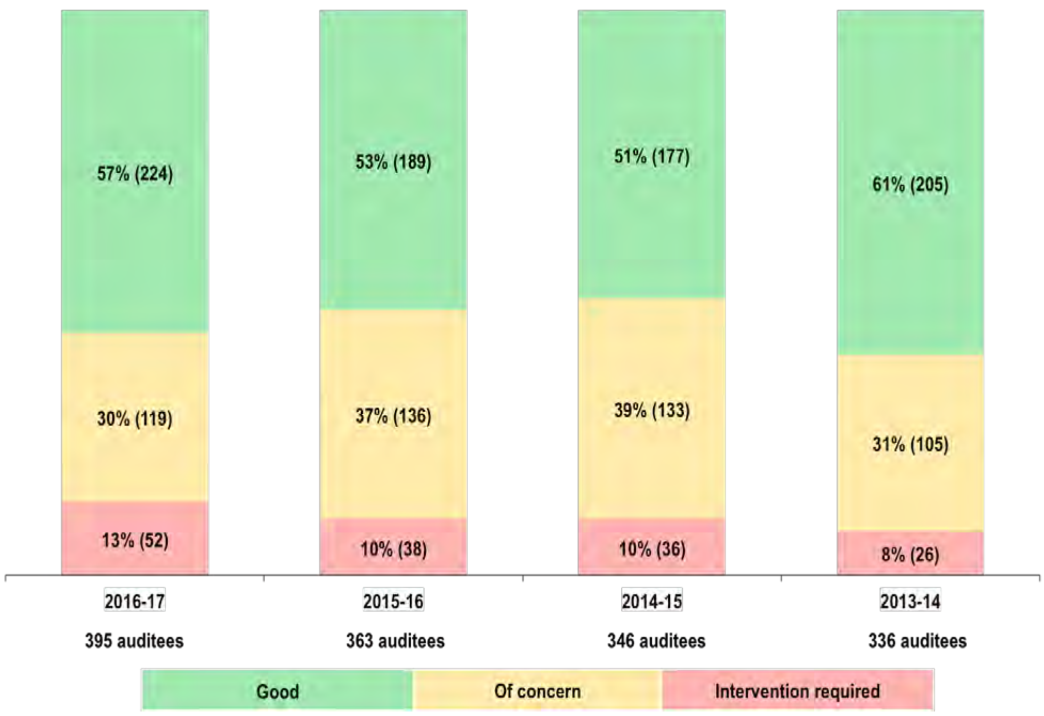
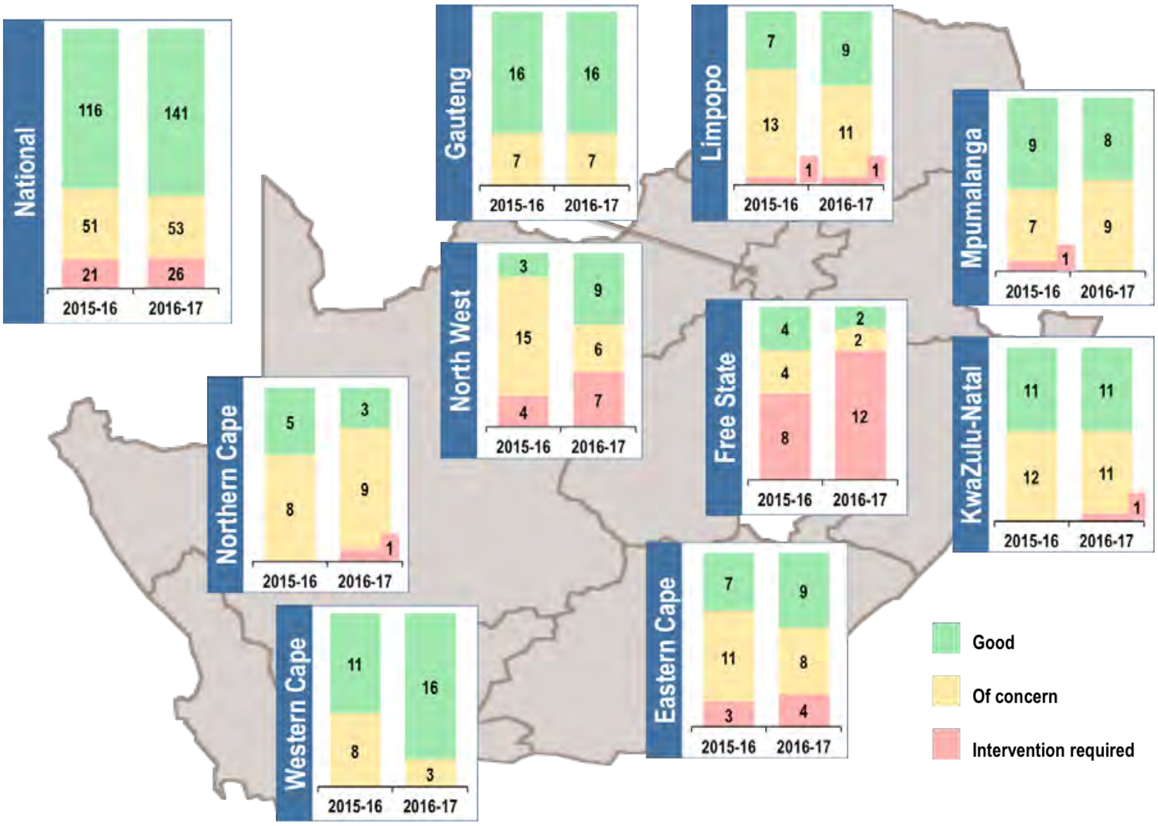


Figure 2: Overview of auditees with indicators of financial health risks



The number of auditees we assessed as having a **good financial health status had increased since 2013-14** (the percentage shows a regression, but it is as a result of a significant increase in the number of auditees being audited since 2013-14). There was also a **slight improvement from 2015-16**. However, the number of **auditees that required intervention doubled in the past four years**, with the main increase being in 2016-17.

As can be seen in figure 2, the provinces with the **highest number of auditees that required intervention** and who had the highest increase from 2015-16 were the Free State (12 auditees) and North West (seven auditees). In the national sphere, the poor quality of the financial statements of the TVET colleges and the concerning financial state of the public entities were the main contributors to the number of auditees requiring intervention.

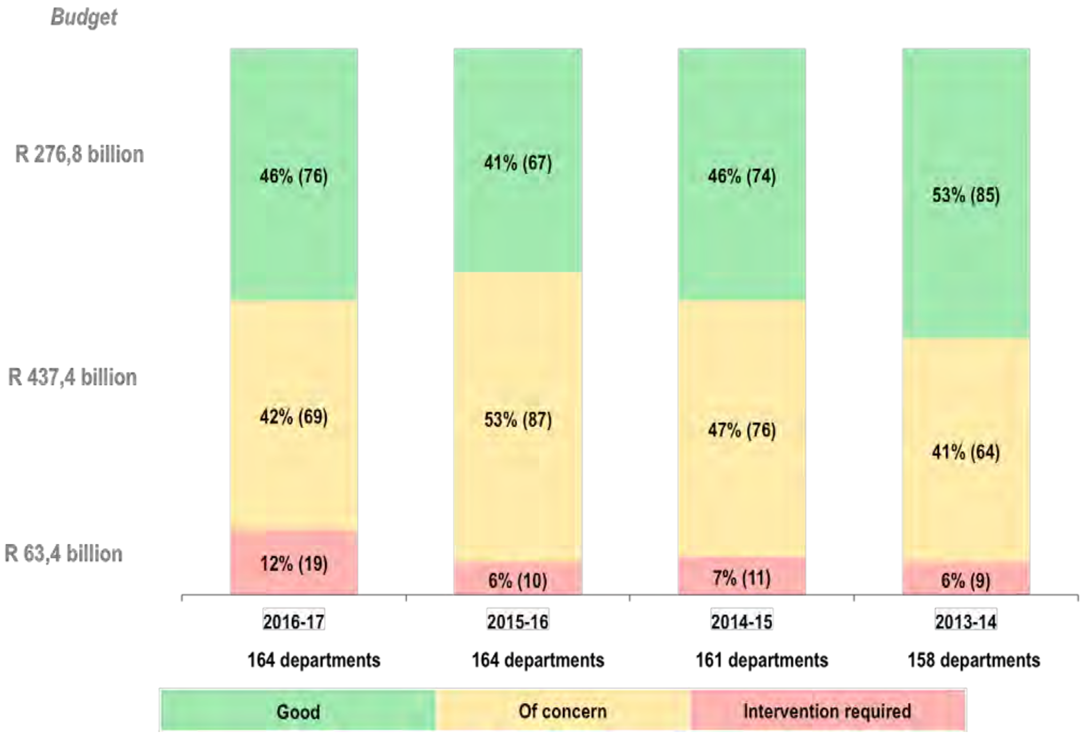
Only in the Western Cape and Gauteng more than 70% of the auditees had a good financial health status.

We provide further details on the status and main financial indicators of departments and public entities in the remainder of this section. Please also refer to section 16 for a provincial perspective.

Financial health and unauthorised expenditure of departments

Figure 3 provides a four-year view of the financial health of departments and also shows the total budget of the departments within each category.

Figure 3: Number of departments with indicators of financial health risks



Since 2013-14, there had been a **regression in the overall financial health of departments**. Although the number of departments with a good status increased slightly from 2015-16, it represented only 36% of the departmental budgets, while the number of departments in financial difficulty almost doubled.

Over the four-year period, 64% of the departments in the Eastern Cape lost their good status, with the Western Cape and Gauteng losing 15% and 13% of departments in this category, respectively. In 2016-17, 92% (12) of the departments in the Free State were assessed as requiring intervention, representing R26,7 billion (98%) of the province's budget.

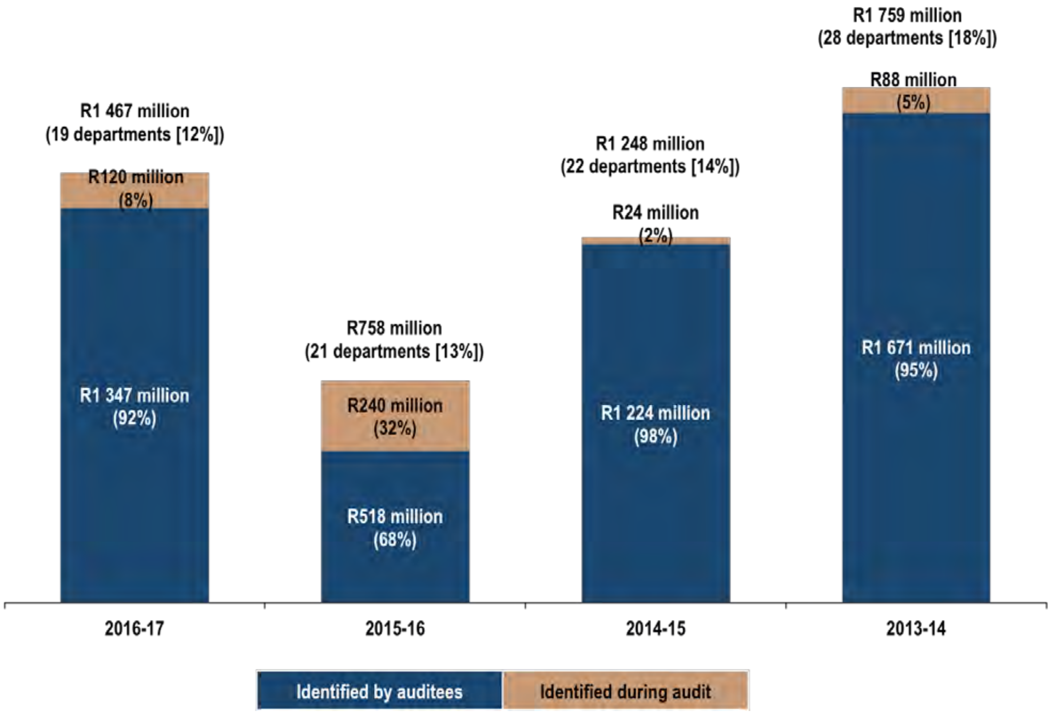
The status of **unauthorised expenditure** also provides a view of the financial health of departments.

What is unauthorised expenditure?

Unauthorised expenditure refers to expenditure incurred by departments that was not spent in accordance with the approved budget.

Figure 4 depicts the extent of unauthorised expenditure over the past four years and the proportion thereof that was identified during the audit and not by the department.

Figure 4: Four-year trend in unauthorised expenditure



As reflected in figure 4, 12% of the departments incurred unauthorised expenditure in 2016-17 – the number of departments decreased steadily and the amount decreased by 16% over the four-year period, but significantly increased by 93% since the previous year. A total of 10 (52%) of the 19 departments that had unauthorised expenditure in 2016-17 also incurred such expenditure in the previous year, five of which had incurred such expenditure for the past four years.

Departments in the following provinces were the **main contributors to the significant increase in unauthorised expenditure from the previous year**:

- Eastern Cape – R175 million (increased from R4 million)
- North West – R105 million (increased from R9 million)
- Mpumalanga – R98 million (increased from R9 million)
- Gauteng – R99 million (increased from R13 million)

Overspending of the budget or main sections within the budget was the reason for 92% (2015-16: 75%) of the unauthorised expenditure. Poorly prepared budgets, inadequate budget control and a lack of monitoring and oversight were some of the reasons for the overspending. Only 8% of the unauthorised expenditure was as a result of expenditure not being used for its intended purpose (at the Department of Water and Sanitation).

Figure 4 also shows that we had identified only 8% of the unauthorised expenditure amount during the audit process, which means that most of the departments have adequate processes to detect and quantify all unauthorised expenditure. This is encouraging and an improvement from the previous year.

The following departments, mostly in the education and health sectors, were the **main contributors** (93%) to unauthorised expenditure in 2016-17:

- Department of Water and Sanitation – R407 million (2015-16: R0)
- Education (Free State) – R238 million (2015-16: R157 million)
- Education (Eastern Cape) – R175 million (2015-16: R0)
- Health (North West) – R100 million (2015-16: R0)

- Education (Mpumalanga) – R97 million (2015-16: R0)
- Education (Gauteng) – R81 million (2015-16: R0)
- Education (KwaZulu-Natal) – R79 million (2015-16: R45 million)
- Education (Northern Cape) – R69 million (2015-16: R0)
- Health (Free State) – R68 million (2015-16: R32 million)
- Health (Northern Cape) – R52 million (2015-16: R93 million)

As detailed in section 9.3, inadequate steps taken by accounting officers to prevent unauthorised expenditure constituted one of the most common material findings on compliance. We reported the findings on compliance as material at 11 departments (7%) (2015-16: 12 [7%]) based on the fact that they had incurred the same type of expenditure in the current and previous years as well as our assessment that adequate controls and processes would have prevented it.

A

Annexure 1 available on our website shows the auditees that had incurred unauthorised expenditure.

We provide further details below on the financial indicators we used to analyse the financial health of departments, but first it is important to understand how the financial analysis of departments is different from that of other auditees and private sector entities.

Departments prepare their financial statements on what is called the **modified cash basis of accounting**. This means that the amounts disclosed in the financial statements are only what had actually been paid during the year and **do not include accruals** (the liabilities for unpaid expenses) at year-end. While this is common for government accounting, it does not give a complete view of the year-end financial position of a department.

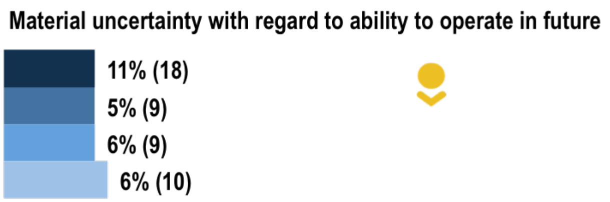
We believe it is important for management to understand the state of their departments' finances, which may not be easily seen in their financial statements – hence we annually **reconstruct the financial statements** at year-end to take into account these unpaid liabilities. It allows us to assess and report to management whether the surpluses they reported are the true state of affairs and whether they have technically been using the following year's budget as a result of overcommitment in a particular year.

The following legend applies to the figures shown:

2016-17	2015-16	2014-15	2013-14

Figure 5 reflects the number of departments that in the past four years disclosed in their financial statements that a **material uncertainty** existed with regard to their ability to operate in the foreseeable future (in other words, as a going concern). We explain what a going concern is in section 4.

Figure 5: Going concern uncertainty



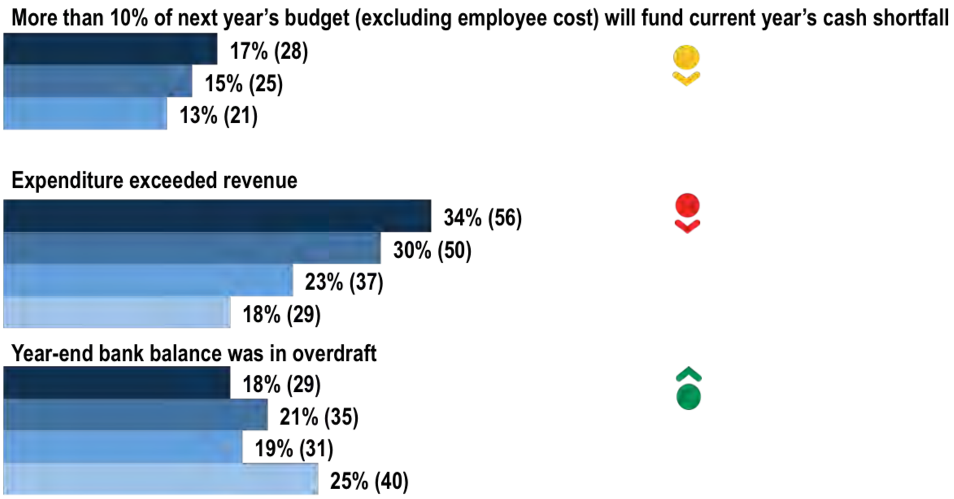
A **going concern uncertainty** existed at 18 departments in 2016-17 (which are responsible for over R63 billion of the budget) – a regression from the previous year and a slight regression since 2013-14.

The departments that reported in 2016-17 that they were in serious financial trouble included:

- three health departments (Eastern Cape, Free State and Northern Cape)
- 12 of the 13 departments in the Free State
- the Department of Water and Sanitation (the Water Trading Entity also reported a going concern uncertainty)
- the Independent Police Investigative Directorate.

Figure 6 shows some of the typical indicators of going concern uncertainty over the past four years, in addition to the revenue management and creditor-payment period indicators detailed later on in this section.

Figure 6: Sustainability indicators



In total, **111 departments (68%) technically had insufficient funds to settle all liabilities that existed at year-end** if the unpaid expenses at year-end were also taken into account. For most of the departments, this would have a minor impact, but 13 departments started the 2016-17 year with more than 10% of their budget effectively pre-spent. However, as shown in figure 6, if the budget for employee cost is not taken into account, **28 (17%) had spent more than 10% of their 2016-17 operating expenditure budget**. Of these 28 departments, all but six were provincial departments and included four education, five health and five public works departments. Those with the highest spending were Human Settlements (Free State) (70%), Cooperative Governance and Traditional Affairs (Mpumalanga) (63%) and Public Works (KwaZulu-Natal) (54%). The national departments included the Department of Home Affairs (which spent 46% of the 2016-17 budget).

An emerging risk is the increased litigation and claims against health departments in most of the provinces. The departments do not budget for such claims, which means that all successful claims will be paid from funds earmarked for the delivery of health services, further eroding the ability of these departments to be financially sustainable.

As per figure 6, the reconstructed financial statements showed that **more than a third of departments incurred a deficit instead of the surplus** they reported; 31 (55%) of these departments also incurred a deficit in the previous year. This shows a significant increase over the past four years. Departments in the Northern Cape and KwaZulu-Natal were the major contributors in this regard, while over half of the departments in the Eastern Cape and the Free State had deficits.

A further matter that requires attention is the 29 departments that had an overdraft at year-end (although there had been an improvement over the four-year period and a slight improvement since the previous year).

Departments receive a budget from government as their key source of revenue. Some departments also generate revenue and depend on the collection of that revenue to provide them with the cash to operate. The main indicators relating to the success of these collections are shown in figure 7.

Figure 7: Revenue management

Almost a fifth of departments estimated in their financial statements that **more than 10% of the outstanding amounts owed to them would not be paid**. This slightly increased over the four-year period.

As part of our analysis, we calculated the average number of days it took departments to **collect debt** they deemed to be recoverable. Almost a quarter of departments had an average debt-collection period of over 90 days in 2016-17. Although this was only a slight improvement over the four years, it was a good improvement from the previous year.

Poor recoverability and slow collection had the greatest impact in the health sector. Table 1 shows the state of collection of mostly patient fees at provincial health departments.

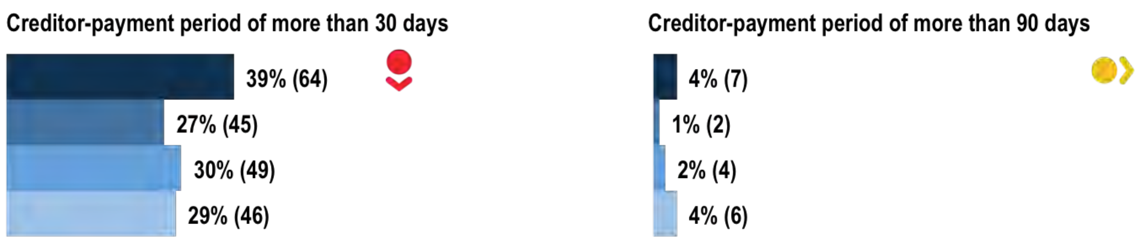
Table 1: Revenue management in the health sector

Province	%	Days	Province	%	Days	Province	%	Days
North West	82	91	Limpopo	95	18	Northern Cape	100	0
Eastern Cape	79	80	Free State	59	267	Gauteng	41	398
Western Cape	37	202	KwaZulu-Natal	12	490	Mpumalanga	0	1 290

(% = Percentage of debt that cannot be recovered Days = Average collection period)

Pressure on the cash flow of departments in turn meant that they took longer to pay their creditors. Figure 8 shows the number of departments with an average **creditor-payment period** of more than 30 days and more than 90 days over the four-year period.

Figure 8: Creditor-payment period



The number of departments with an extended payment period over 30 days significantly increased over the four-year period and since the previous year. The payment period over 90 days remained stagnant over the four-year period with a slight regression from the previous year.

More than half (54%) of the departments in Mpumalanga had a payment period over 30 days, closely followed by the Eastern Cape at 50% as well as the Free State and the Northern Cape at 46% and the national departments at 43%. Health and Infrastructure Development in Gauteng on average took the longest of all the departments to pay their creditors at 171 and 129 days, respectively.

As reported in section 9, the inability of auditees to pay within 30 days was one of the most common compliance findings we had raised. Delayed payments affect the cash flow of the suppliers government is doing business with and are in sharp contrast with the objectives of stimulating the economy and supporting especially smaller businesses.

Although delayed payments are typically as a result of poor controls and processes, it can be concluded that the financial difficulty of some departments and the lack of cash to honour their obligations (as described earlier in this section) are also contributing factors in this regard.

Overall, there is an emerging trend of departments failing to manage their finances properly. Some departments are not paying their creditors when their budgets start running out and thereby avoid unauthorised expenditure, but the payments then happen in the following year, effectively using money intended for other purposes. Some departments overspend on their budgets and still have outstanding liabilities at year-end. This continuing 'rollover' of budgets is having a negative impact on departments' ability to pay creditors on time and to deliver services. The education and health departments are affected the most and their inability to deliver services will have an impact on the most vulnerable in society.

The signs of financial failure in the Free State should receive urgent attention. The provincial overview in section 16 provides more detail in this regard.

Financial health of public entities

Section 4 discusses the major concerns we have identified regarding the financial health of SOEs. The analysis in this section excludes these SOEs to give a view of the state of the other entities, which include constitutional institutions, government business enterprises, trading entities, other public entities that are not profit-driven, and the TVET colleges.

Figure 9 provides a four-year view of the financial health of these public entities and also shows the total budget of the entities within each category.

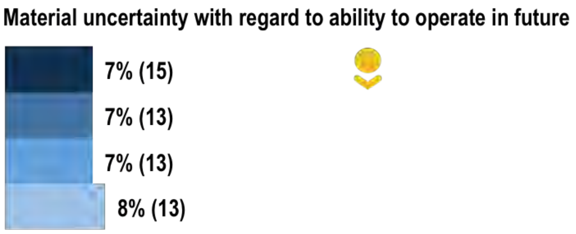
Figure 9: Number of public entities with indicators of financial health risks

The percentage of public entities we assessed as having a good financial health status slightly decreased from 67% in 2013-14 to 66% in the current year, but improved from the previous year. Public entities generally performed better than departments, but we are concerned about the public entities in North West (seven of their nine entities had serious financial difficulties and the financial statements of two were so poor that a reliable assessment could not be done but there were indicators of financial problems). Regarding the 45 TVET colleges that we had audited, 16 were of concern and 10 had poor financial statements that could not be assessed reliably. The other public entities that required intervention included the Unemployment Insurance Fund and the Road Accident Fund.

We provide further details below of the main financial indicators used for the assessment of public entities over the four-year period. The following legend applies to the figures shown:

Figure 10 reflects the number of public entities that in the past four years disclosed in their financial statements that a material uncertainty existed with regard to their ability to operate in the foreseeable future (in other words, as a going concern).

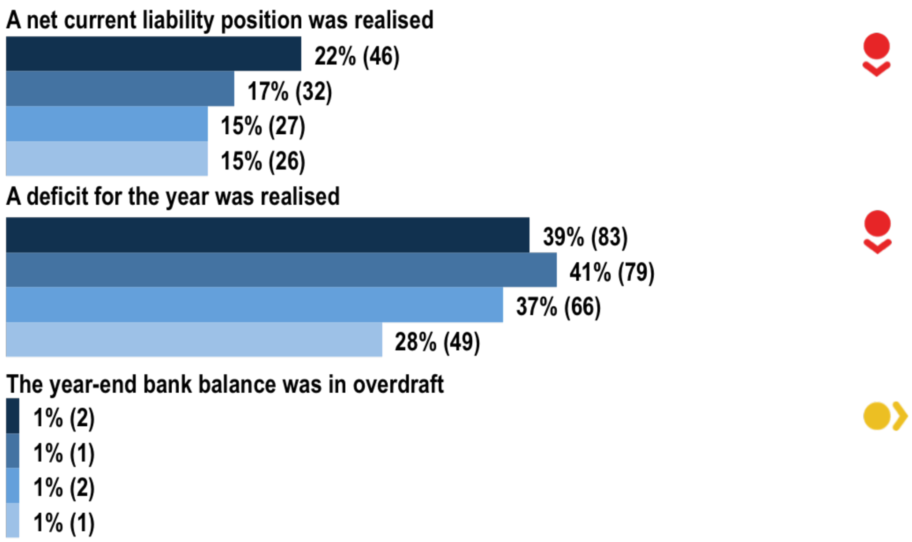
Figure 10: Going concern uncertainty



A **going concern uncertainty** existed at 15 of the public entities in 2016-17 – a slight increase since 2013-14 and 2015-16. This included six public entities in North West as well as the Coega Development Corporation, Road Accident Fund, Public Protector and Water Trading Entity.

Figure 11 shows some of the typical indicators of going concern uncertainty over the past four years, in addition to the revenue management and creditor-payment period indicators detailed later on in this section.

Figure 11: Sustainability indicators



There had been a regression since 2013-14 and a slight regression since the previous year in the number of public entities whose current liabilities exceeded their current assets, which raises a concern over their ability to repay their current liabilities in the short term. This was caused by cash-flow problems (mainly due to poor debt collection and the inability to pay creditors).

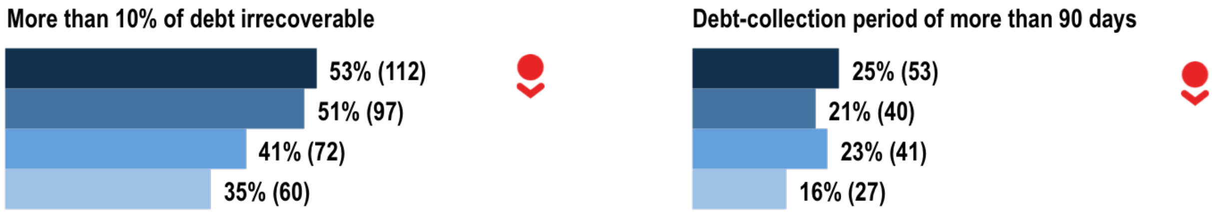
During 2016-17, 39% of the public entities incurred a **net deficit**. These included the Competition Commission, Independent Regulatory Board for Auditors, National Skills Fund, Road Traffic Management Corporation and South African Social Security Agency as well as 56% of the TVET colleges we had audited.

The number of public entities with year-end bank balances in overdraft had remained unchanged since 2013-14.

Even though the majority of public entities that incurred deficits for the financial year would be able to continue their operations, the negative indicators raise concerns about the financial viability of some and the pressure to acquire additional funding from government.

One of the main reasons for the failing financial health of public entities is inadequate **revenue management**. The main indicators over the past four years in this regard are reflected in figure 12.

Figure 12: Revenue management indicators



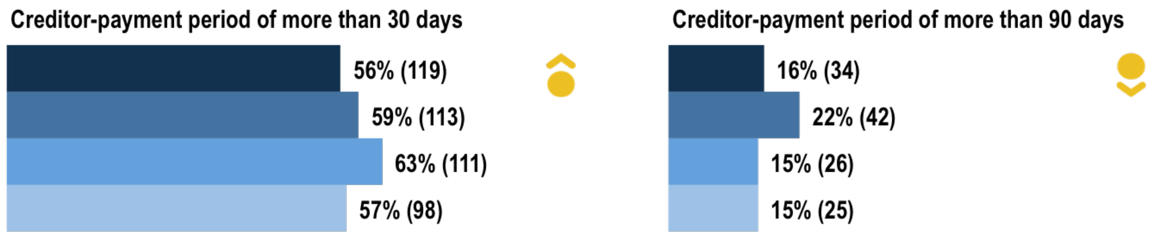
Just over half of the public entities estimated in their financial statements that more than 10% of the outstanding amounts owed to them would not be paid, which had seen a steady increase since 2013-14. A total of 65 (58%) of these 112 public entities estimated that more than 50% of the outstanding amounts owed to them would not be paid, which included 33 of the TVET colleges as well as the Financial Services Board, National Credit Regulator and Special Investigating Unit.

As part of our analysis, we calculated the average number of days it took public entities to **collect debt** they deemed to be recoverable. A quarter of the public entities had an average debt-collection period of over 90 days in 2016-17. This was a slight regression from the previous year.

The root causes of long-outstanding debt, which places revenue funds under pressure and affect the ability of public entities to operate, remain poor revenue-collection and debt-management practices and the poor economic climate.

Extended collection periods put the cash flow of public entities under significant pressure, which in turn meant that they took longer to pay their creditors. Figure 13 shows the number of public entities with an average **creditor-payment period** of more than 30 days and more than 90 days over the four-year period.

Figure 13: Creditor-payment period



Over half of the public entities took more than 30 days to pay their creditors, with limited movement over the four years. These numbers significantly decreased when assessed over 90 days, however, as only 34 auditees took more than 90 days to pay their creditors – a slight increase over the four years but a decrease from the previous year.

Late payments were more common in public entities than in departments. Public entities with extended creditor-payment periods are running the risk of key suppliers discontinuing their services, which may have a significant impact on their operations and ability to deliver services or continue with their business.

Conclusion

The budget and performance planning processes should be informed by a solid analysis and forecast based on credible historical information and knowledge of the funding constraints and expected performance pressures. Auditees in financial difficulty should set clear targets for improvement and plan systematically towards achieving these (**PLAN**).

Financial discipline is required to curtail spending and ensure that the best financial decisions are made. This extends to beyond the chief financial officer and finance unit to procurement practices by all divisions, executive-level decisions and human resource (HR) management, among other (**DO**).

The financial position of departments will only improve if expenditure is more effectively monitored in-year, as and when incurred (and not just when paid), and by improving systems to promptly account for liabilities incurred. The National Treasury, provincial treasuries and relevant portfolio committees should monitor actual spending patterns and identify the departments with serious cash shortfall issues to intervene where necessary (**CHECK**).

6 Status of progress on the audit outcomes

6.1 Overall audit outcomes

National and provincial government consists of 169 departments and 599 public entities. The audit outcomes of 97 public entities audited by private auditors, 67 dormant public entities and 19 public entities with different reporting cycles are not included in the analysis presented in this report. As part of our audit methodology, we classified 163 public entities as small auditees based on the size and nature of their business. The audit outcomes of these public entities are also not included in this general report, but are published in the annexures available on our website.

We set the cut-off date for inclusion of the audit outcomes in this report as 31 August 2017. By this date, 26 audits were still outstanding. More information in this regard is provided in section 6.2.

Figure 1 reflects the audit outcomes of the remaining 422 auditees; figures 2 and 3 show the outcomes for departments and public entities, respectively; while table 1 analyses the movement in audit outcomes from the previous year.

Figure 1: Audit outcomes of auditees

Figure 2: Audit outcomes of departments

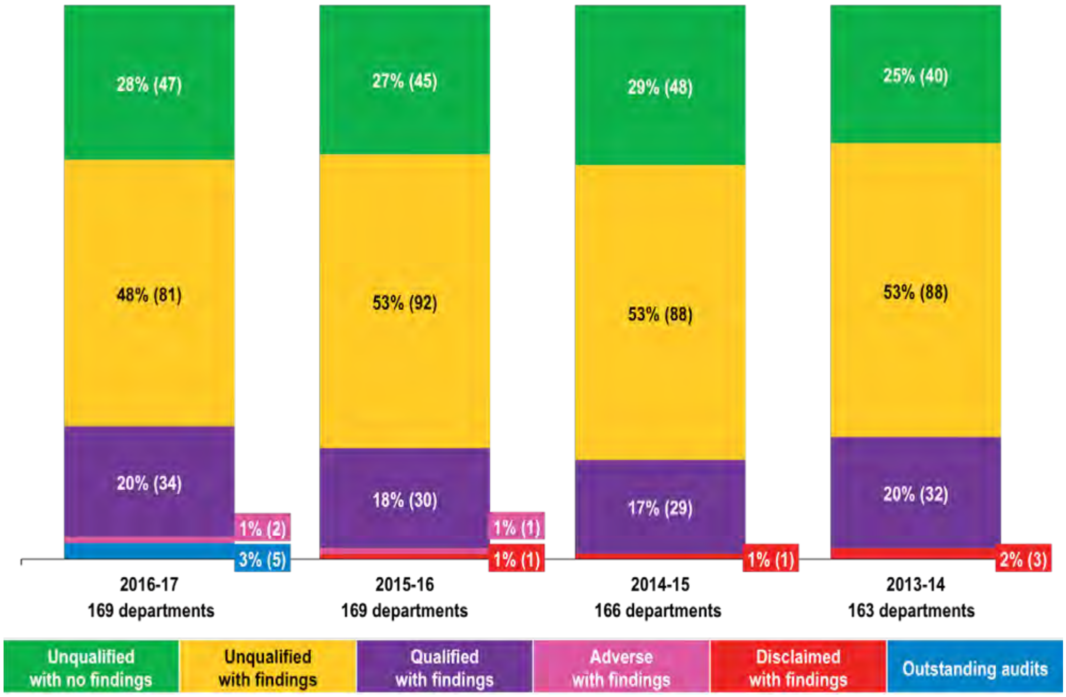


Figure 3: Audit outcomes of public entities

Table 1: Movement in audit outcomes from 2015-16 to 2016-17

Audit outcome / Movement	60 Improved	259 Unchanged	47 Regressed	30 New auditee	16 + 10 Outstanding audits (prior year audit outcome)
Unqualified with no findings = 126	9 (DEP) 20 (PE) 1 (DEP) 1 (PE)	37 (DEP) 47 (PE)		11 (PE)	1 (DEP) 3 (PE)
Unqualified with findings = 179	5 (DEP) 13 (PE)	71 (DEP) 59 (PE)	5 (DEP) 18 (PE)	8 (PE)	1 (DEP) 4 (PE)
Qualified with findings = 72	1 (DEP) 9 (PE)	21 (DEP) 14 (PE)	1 (DEP) 11 (DEP) 8 (PE)	7 (PE)	3 (DEP) 1 (PE)
Adverse with findings = 9	1 (PE)	1 (DEP) 2 (PE)	1 (DEP) 1 (PE)	3 (PE)	
Disclaimed with findings = 10		7 (PE)	1 (PE) 1 (PE)	1 (PE)	3 (PE)

DEP – departments PE – public entities Colour of the number indicates the audit opinion from which the auditee has moved.
Of the 26 outstanding audits, three audits remain outstanding since the 2015-16 financial year, with seven new audits outstanding.

The 26 outstanding audits relate to 16 auditees of which the 2016-17 audits had not been completed plus 10 auditees made up of three auditees whose 2015-16 audits were also still outstanding and seven auditees that we audited for the first time in 2016-17.

There had **been an improvement in the overall audit outcomes** since 2013-14 with only a **slight improvement from the previous year**. Figures 2 and 3 show that **public entities improved over the four years** but **departments showed only a slight improvement**. In total, 31 departments (20%) improved their outcomes, but 24 (15%) regressed and 103 (65%) remained the same. The movements for public entities were that 64 (35%) improved their outcomes, 28 (15%) regressed and 91 (50%) remained the same.

Overall, 10% of departments improved their outcomes from the previous year, 11% regressed and the remainder did not change – which means that there was **a slight regression in the outcomes of departments from the previous year**. **Public entities showed a slight improvement** from the previous year, as 22% improved and 14% regressed.

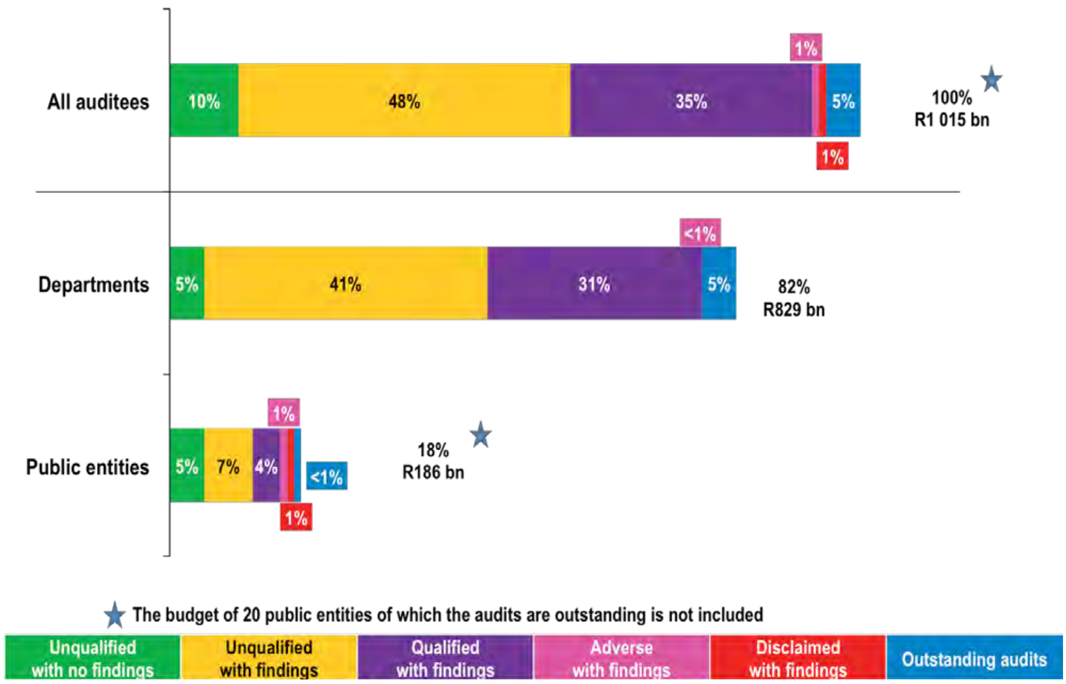
The number of **auditees with clean audits** increased to 126 (30%), of which 57 had also received clean audit opinions in 2013-14. These include Parliament, provincial treasuries and legislatures, and 65% of the auditees in the Western Cape. Maintaining a strong control environment and being vigilant about responding correctly and timeously to any changes in accounting standards or legislation were some of the key contributors to sustaining the outcomes. The clean audits in 2016-17 represented 31% of the national departments, 28% of the provincial departments, and 34% each of national and provincial public entities.

In total, 67% (84) of the **auditees with clean audit opinions** in 2015-16 obtained this outcome again in 2016-17, which is an encouraging sign that improvements at these auditees are sustainable. A total of 31 auditees moved into this category but unfortunately 25 auditees lost their clean audit status, resulting in only a slight increase in the number of auditees with clean audit opinions.

Overall, 130 (73%) of the 179 auditees that received an **unqualified audit opinion with findings** in 2016-17 had recorded the same opinion in 2015-16. Only 29 of these auditees could progress to a clean audit this year. Although some progress had been made towards financially unqualified audit opinions as detailed in section 7, auditees still need to address their material findings on the quality of the performance reports and compliance with legislation. The leadership is responding too slowly to our recommendations to improve these critical aspects of administration.

The **expenditure budget** in 2016-17 was R1 015 billion, of which R927 billion was operating expenditure and R88 billion was capital expenditure. Figure 4 reflects the audit outcomes of departments and public entities versus their budget allocations, rounded to the nearest billion.

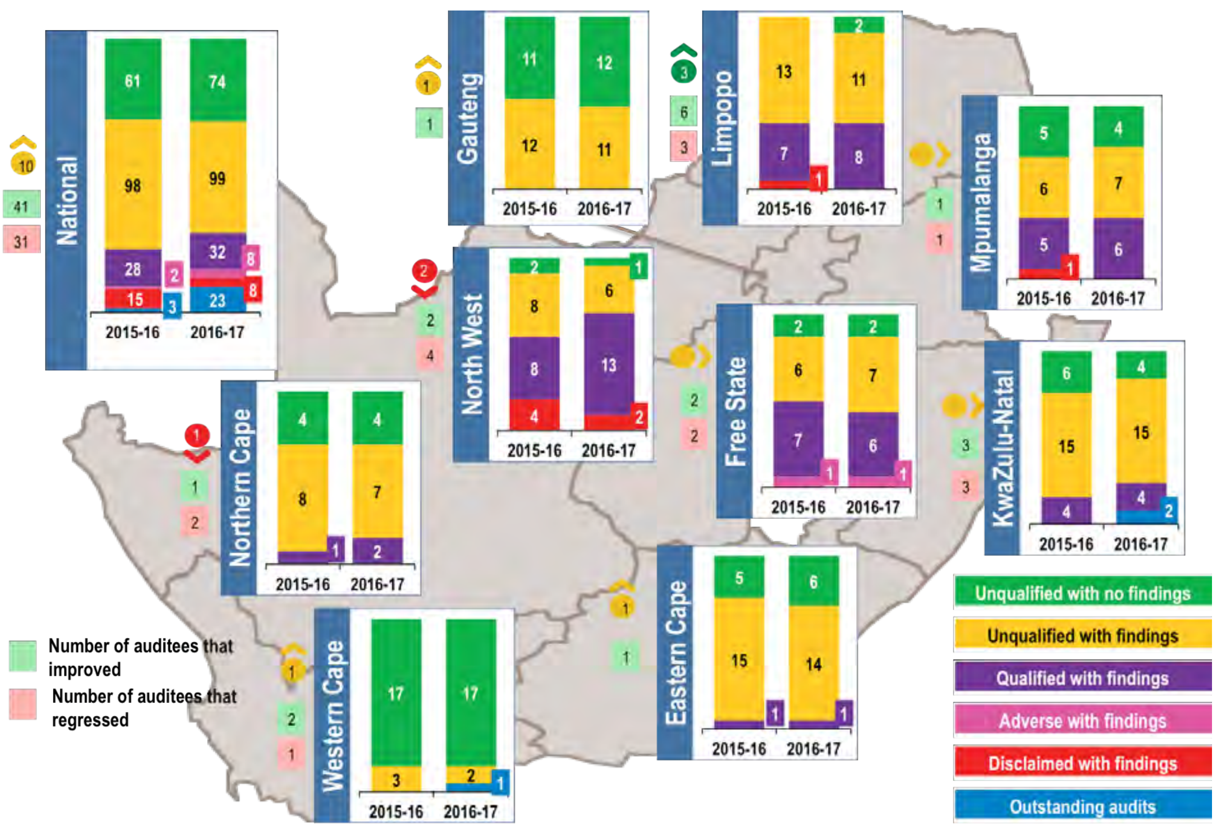
Figure 4: Audit outcomes versus budget allocations



As can be seen in figure 4, the 126 auditees with clean audit opinions represented only 10% of the total expenditure budget. Only 58% of the budget was accounted for in financial statements that fairly presented the finances of the auditees and could be relied upon by the users thereof.

Figure 5 illustrates the national and provincial audit outcomes of 2015-16 compared to those of 2016-17 for all auditees.

Figure 5: National and provincial audit outcomes (all auditees)



The audit outcomes of Limpopo improved, with a slight improvement in the national sphere and in three provinces, while two provinces regressed and three remained unchanged from the previous year. The provinces with the highest percentage of auditees (departments and public entities) with clean audit opinions in 2016-17 were the Western Cape (85%) and Gauteng (52%). Common in both provinces was the role of the leadership in instilling a culture of accountability and expecting nothing less than sound administration. The provinces with the poorest outcomes, based on the percentage of auditees with disclaimed and adverse opinions or outstanding audits, were North West (9%), KwaZulu-Natal (8%) and the Free State (6%), but the majority of the poor outcomes were in the national sphere (16%). A lack of accountability and commitment towards clean administration was evident in North West and the Free State – the audit outcomes in these provinces regressed over the four years.

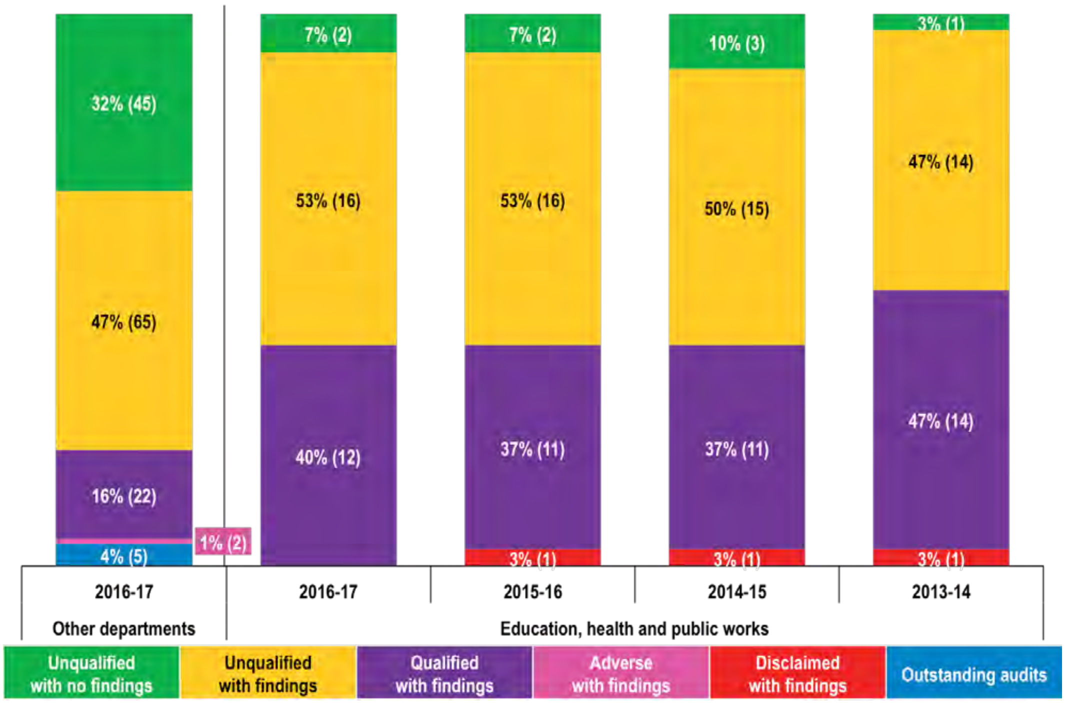
The provincial overview in section 16 provides detail on the reasons for the audit outcomes in the provinces.

Education, health and public works

In 2016-17, the expenditure of the national and provincial departments of education, health and public works contributed to almost 38% of the total spending by auditees.

Figure 6 shows the audit outcomes of these departments versus those of the other departments.

Figure 6: Education, health and public works versus other departments



In total, 40% of the education, health and public works departments' financial statements received a financially qualified opinion compared to 17% of the other departments. Except for two clean audits, all these departments had material findings on the quality of their performance reports and/or compliance with legislation. The audit outcomes slightly improved over the past four years with the Limpopo education department improving from disclaimed opinions for three years to a qualified opinion in 2016-17. This improvement can be attributed to the appointment in 2016-17 of an official from the provincial treasury to lead the administration team who set the right tone at the top and, through collaborating with departmental officials, could produce improved results.

These sectors receive a substantial portion of the budget and are responsible for implementing key programmes to improve the health and welfare of citizens. Their poor audit outcomes should receive urgent attention from all role players to ensure accountability and improved service delivery.

Conclusion

Improvements in **audit outcomes** can be achieved if all elements of the **PLAN**+**DO**+**CHECK**+**ACT** cycle are implemented. Section 15 provides recommendations in this regard.

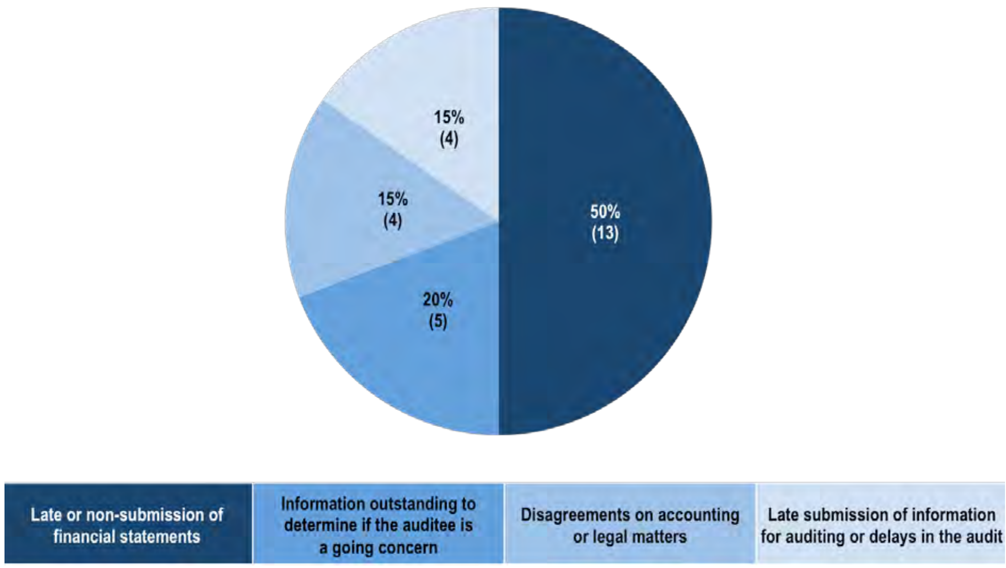
A On our website, annexure 1 lists all auditees with their current and prior year audit outcomes, while annexure 3 lists the audit outcomes for the past five years.

6.2 Outstanding audits

We set the cut-off date for inclusion of the audit outcomes in this report as 31 August 2017. By this date, **26 audits had not been completed** (6% of our total national and provincial audits), compared to 11 audits that had been outstanding at the same time last year. Of these, 23 were national auditees (four departments and 19 public entities).

Tables 1 and 2 provide detail on the **reasons for the audits not having been finalised**, with the main reasons being indicated in figure 1.

Figure 1: Main reasons for the outstanding audits



Some of the outstanding audits were as a result of the contestation we experienced, as described in section 2.

Table 1 lists the 19 audits that had not been completed by the date of this report and provides the reasons for the late finalisation.

Table 1: Outstanding audits

No.	Auditee	Portfolio	Reason
1	Defence	Defence and military veterans	Separate financial statements were prepared and submitted on 31 May 2017 for the Department of Defence and the Special Defence Account. However, the department received a letter from the National Treasury on 28 June 2017 indicating that the Special Defence Account is not a separate legal entity, which meant that their financial information should be consolidated into the financial statements of the department. The department did not agree with this position and obtained a legal opinion on 28 August 2017 from the state law advisors in this regard. It confirmed that the Special Defence Account is not a separate legal entity. Interactions are currently still underway between the National Treasury and the department regarding the appropriate accounting treatment of the Special Defence Account. The final outcome of this matter is delaying the finalisation of the audit of the department.
2 3 4	SAA Air Chefs SOC Limited SAA Technical SOC Limited	Finance (treasury)	The auditees did not submit financial statements, as management and the board could not conclude on whether these companies were a going concern.
5	Mango Airlines SOC Limited	Finance (treasury)	Financial statements were received on 31 May 2017 but the finalisation of the audit is dependent on the finalisation of the SAA going concern assessment.
6	South African Revenue Service (Own Account)	Finance (treasury)	A legal disagreement on the approval of performance bonuses is delaying the finalisation of the audit.
7	SA Express	Public enterprises	The 2015-16 audit of SA Express was finalised late due to the processes that needed to be finalised between SA Express, the Department of Public Enterprises and the National Treasury on a government guarantee. This had an impact on finalising the financial statements, which were then submitted on 4 July 2017, but without all the supporting documentation. The final financial statements were only submitted on 31 August 2017.
8	Compensation Commissioner for Occupational Diseases	Health	The auditee had a huge backlog due to not having captured data files for mine workers to enable a valuation of the provision for compensation commission claims in 2010-11. The capturing of backlog data took a couple of years to resolve and actuarial valuations needed to be done. Because the initial backlog was six years, the auditee is still catching up with submitting backlog financial statements. No financial statements have been submitted since 2012-13.
9 10 11	East Cape Midlands TVET College Northern Cape Rural TVET College Tshwane North TVET College	Higher education and training	No financial statements were submitted for the following reasons: East Cape Midlands TVET College – instability in the position of chief financial officer affecting the preparation of financial statements. Northern Cape Rural TVET College – system problems experienced close to year-end. Tshwane North TVET College – inadequate financial systems and internal controls.
12	Sedibeng TVET College	Higher education and training	Financial statements were only received on 4 September 2017 due to instability in the accounting officer position and a lack of oversight to keep finance staff accountable for complete and accurate asset records.
13	Tshwane South TVET College	Higher education and training	The auditee did not have a complete and accurate fixed asset register. The reconstruction of the asset register took longer than anticipated, which delayed the submission of the financial statements. Financial statements were only received on 3 July 2017.
14	Autopax	Transport	We identified a going concern issue that is dependent on the holding company, Prasa, providing subordination and approved financial commitments, which is delaying the finalisation of the audit.
15	Driving Licence Card Account	Transport	A disagreement on SCM findings we raised is delaying the finalisation of the audit.
16	Prasa	Transport	No financial statements were submitted as there is no board at the auditee.
17	South African Maritime Safety Authority	Transport	Financial statements were only submitted on 7 June 2017, as the auditee did not have all the supporting documentation ready.

No.	Auditee	Portfolio	Reason
18	South African National Roads Agency	Transport	The audit has been delayed as information is outstanding to determine whether the agency is a going concern.
19	Agriculture	Western Cape	A disagreement on the accounting for certain transfers made by the department is delaying the finalisation of the audit.

Table 2 includes the **seven audits that were finalised after 31 August** – it provides the reasons for the late finalisation, the outcomes of the audit and the unauthorised, irregular as well as fruitless and wasteful expenditure incurred (the 2015-16 amounts are indicated in *italics*).

Table 2: Audits subsequently finalised

Number	Auditee	Reason for late finalisation of audit	Movement from previous year's audit outcome	2016-17 audit outcomes			2015-16 audit outcomes			2016-17 unauthorised, irregular and fruitless and wasteful expenditure		
				Audit opinion	Predetermined objectives	Compliance with legislation	Audit opinion	Predetermined objectives	Compliance with legislation	Unauthorised expenditure R million	Irregular expenditure R million	Fruitless and wasteful expenditure R million
1	Cooperative Governance	Inability to perform required work at an interim phase as the auditee was still trying to address prior year qualifications on the community work programme. Thus, work normally concluded by May could only be performed subsequent to the submission of financial statements. This was the majority of audit work on the community work programme, which included regional visits.	Unchanged		R	R		R	R	0 *(0)*	330 *(344)*	0,35 *(0)*
2	International Relations and Cooperation	Department needed to do additional work on assets.	Improved		N	R			R	34 *(167)*	368 *(344)*	2,7 *(5,5)*
3	Independent Development Trust	Delay in submission of supporting documentation.	Unchanged		R	R		R	R	0 *(0)*	4,9 *(6)*	0 *(4,9)*
4	Property Management Trading Entity	Late submission of financial statements as the auditee was required to provide financial statements in full compliance with Generally Recognised Accounting Practice for the first time during the current year. The implementation process of the deemed cost allocation for immovable assets needed to be addressed.	Regressed		R	R		N	R	0 *(0)*	268 *(510)*	0,2) *(0,07)*
5	Transport	Department needed to do additional work on eNatis assets.	Improved		A	N		A	R	177 *(0)*	94 *(123)*	1 *(0,1)*
6	Ithala Development Finance Corporation	Delay in banking licence exemption from minister of Finance.	Regressed			N				0 *(0)*	23 (0,6)	0 *(0,05)*
7	Ithala	Delay in banking licence exemption from minister of Finance.	Regressed			N				0 *(0)*	2,6 *(0,6)*	0 *(0)*

Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Addressed (A)	New (N)	Repeat (R)

Traditional leaders and councils

The Traditional Leadership and Governance Framework Act called for the establishment of traditional councils. It stipulates that once the premier has recognised a traditional community, that community must establish a council in line with the principles set out in provincial legislation. The provincial legislation, which is in place in all provinces except the Western Cape that does not currently have recognised traditional communities, regulates the performance and functions of traditional councils by requiring that the council at least keeps proper records and has its financial statements audited. It also requires the council to meet at least once a year with the community to give account of its activities and finances.

Except for Mpumalanga's legislation, all the legislation specifically requires us to audit the 'books of accounts' or 'financial statements' of these structures. There is no consistency in the legislation on the nature of the 'records' that must be submitted to us for auditing, and in most provinces the legislation does not prescribe the accounting framework to be used.

There are an estimated 940 formally recognised traditional authorities across the eight provinces, predominantly in rural areas where there are very few or no people with the requisite financial skills to assist these authorities to prepare financial records – especially if a sophisticated accounting framework is used. The National Treasury is defining the most appropriate accounting frameworks for these councils. In the absence thereof, **most councils are not preparing any accounts or financial statements that we can audit**.

In North West, one central bank account is maintained by the provincial treasury with individual ledger accounts, comprising the various trust accounts and a total of 92 traditional authority accounts. The financial statements of the North West Tribal and Trust Fund (D-account) have remained outstanding since 2001, with the last audit as at 31 March 2001 resulting in a disclaimed opinion.

In Limpopo, there is a similar set-up with a central bank account also maintained by the provincial treasury. The provincial treasury currently compiles an income and expenditure statement for the trust account. The source for the preparation of this statement is the transactions appearing in the bank statements and, as a result, we were not in a position to provide assurance that all monies that should have been collected had in fact been collected. This was primarily due to the poor status of record keeping and the lack of adequate monitoring controls at the individual tribal authorities. Furthermore, the books and accounts of the individual tribal authorities have not been submitted for auditing since 1994.

We have raised our concerns on the lack of accountability for the activities and finances of the traditional councils at provincial level as well as with the National Treasury and the Departments of Cooperative Governance and of Traditional Affairs. It is expected that the Traditional and Khoi-San Leadership Bill will eventually clear some of the inconsistencies and uncertainties but urgent intervention is required by national and provincial role players to ensure that the funds allocated to, or generated for, traditional communities are accounted for.

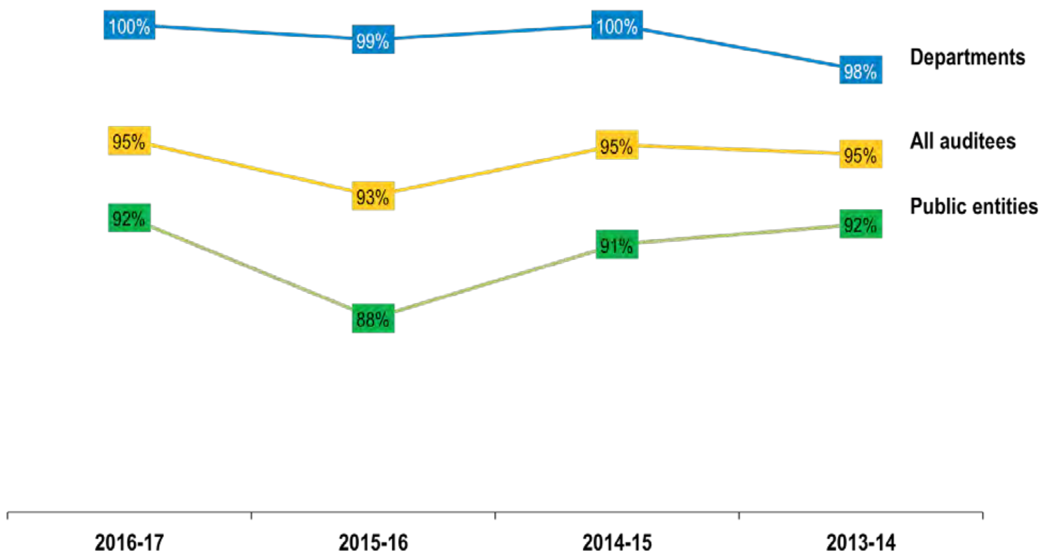
7 Financial statements

7. *Financial statements*

Auditees account for government spending through their financial statements. Committees of Parliament and the legislatures, oversight and monitoring departments (such as treasuries) and other users such as the public, lenders and banks use the financial statements to assess the financial position of the auditees and how money was made and spent in the year. It is an important accountability mechanism and our responsibility is to provide assurance to these users that the financial statements are a fair and true reflection.

Figure 1 provides a four-year overview of the overall percentage of auditees that had submitted their financial statements for auditing by the legislated date (orange line), while the blue and green lines depict the same for departments and public entities, respectively.

Figure 1: Submission of financial statements



In total, 402 (95%) of the auditees had **submitted their financial statements** for auditing by 31 May (or by 31 March in the case of TVET colleges). This percentage remained unchanged over the four-year period but was a slight improvement from the previous year. Lower submission rates were evident at public entities. The main reasons for the late submissions were a breakdown in the control environment, which led to the entities not being able to prepare financial statements on time, and the inability of management to conclude on whether the companies were a going concern. Of the 20 public entities that did not submit financial statements on time, eight had not done so by the date of this report, of which two were TVET colleges and four were part of the SAA group. Refer to section 6.2 for further detail on the outstanding audits.

Figure 2 provides a four-year overview of audit opinions on the financial statements and the percentage of auditees that submitted financial statements that were not materially misstated (orange line). Figures 3 and 4 provide the same overview for departments and public entities, respectively.

Figure 2: Four-year trend – audit of financial statements

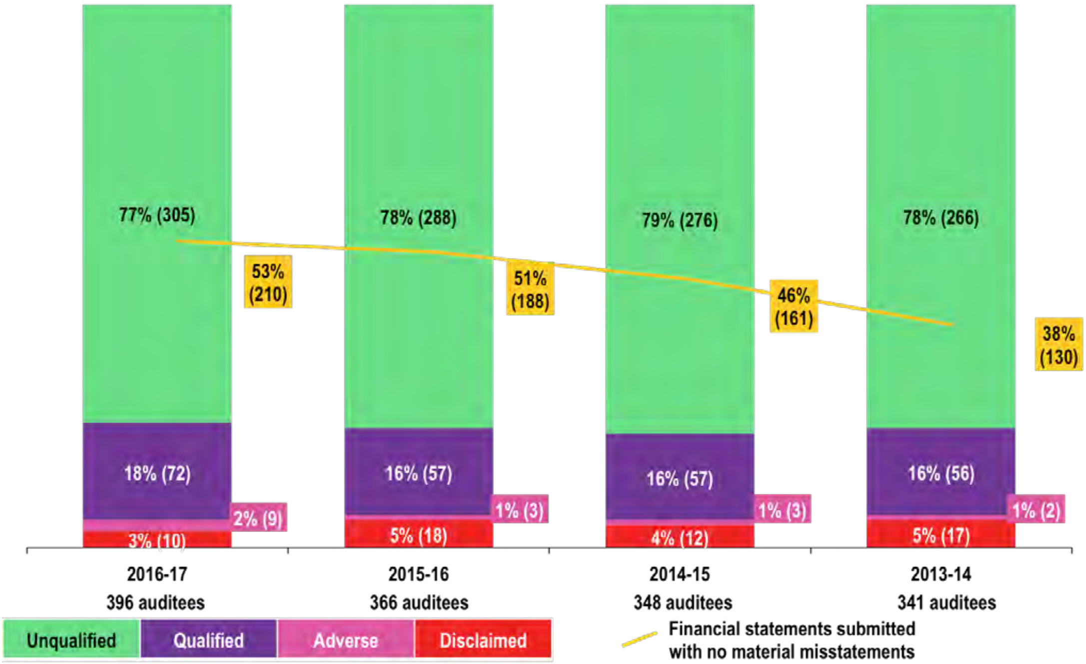


Figure 3: Audit of financial statements – departments

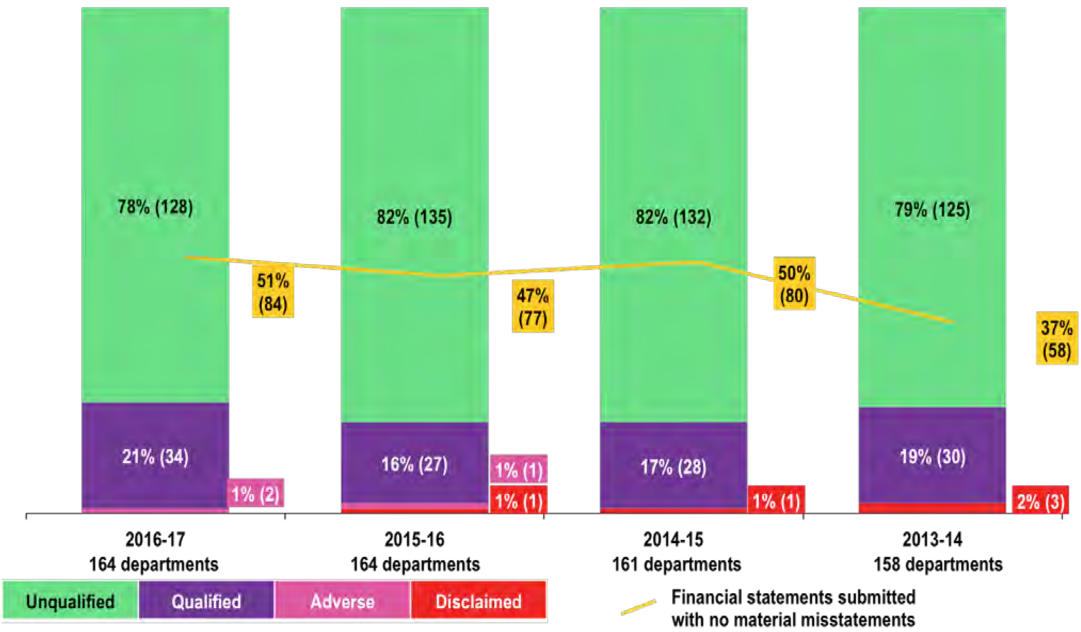


Figure 4: Audit of financial statements – public entities

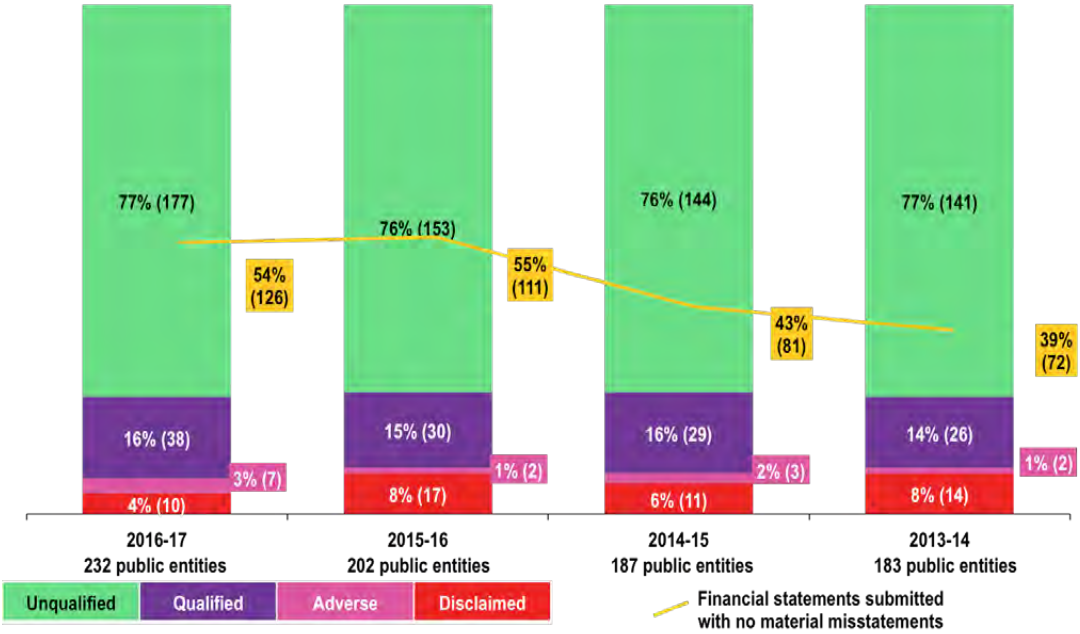


Figure 2 shows that the number of auditees with **unqualified audit opinions on their financial statements** had increased since 2013-14 (the percentage shows a regression, but it is as a result of a significant increase in the number of auditees being audited since 2013-14), with a further increase since the previous year. However, a slight regression was evident for departments since 2015-16, as 18 departments regressed (including eight national departments).

Only 53% of the auditees could provide us with financial statements that contained **no material misstatements** in 2016-17, which was an improvement from 2013-14 and a slight improvement over the previous year. This means that 44 departments (27%) and 51 public entities (22%) received a financially unqualified audit opinion only because they corrected all the misstatements we had identified during the audit. A total of 36 departments and 55 public entities were unable to make the necessary corrections to their financial statements, which resulted in qualified, adverse or disclaimed audit opinions (collectively called 'modified opinions'). Of the 55 public entities that were unable to do so, 44% were TVET colleges. The main reason for not making such corrections was the unavailability of information, or incomplete information or documentation to determine the correct amounts to be reflected in the financial statements.

Countrywide, 40% of the financial statements of the national and provincial departments of education, health and public works received a modified opinion. Compared to 2015-16, Public Works (Northern Cape) regressed from unqualified to qualified, while Health (Free State) and Education (Limpopo) improved from qualified to unqualified and disclaimed to qualified, respectively. The provincial overview in section 16 provides some insight into the reasons for the movements.

Table 1 shows the percentage of auditees in national and provincial government that submitted quality financial statements for auditing (in other words, with no material misstatements) and the outcomes after corrections had been made.

Table 1: Status of financial statements in national and provincial government

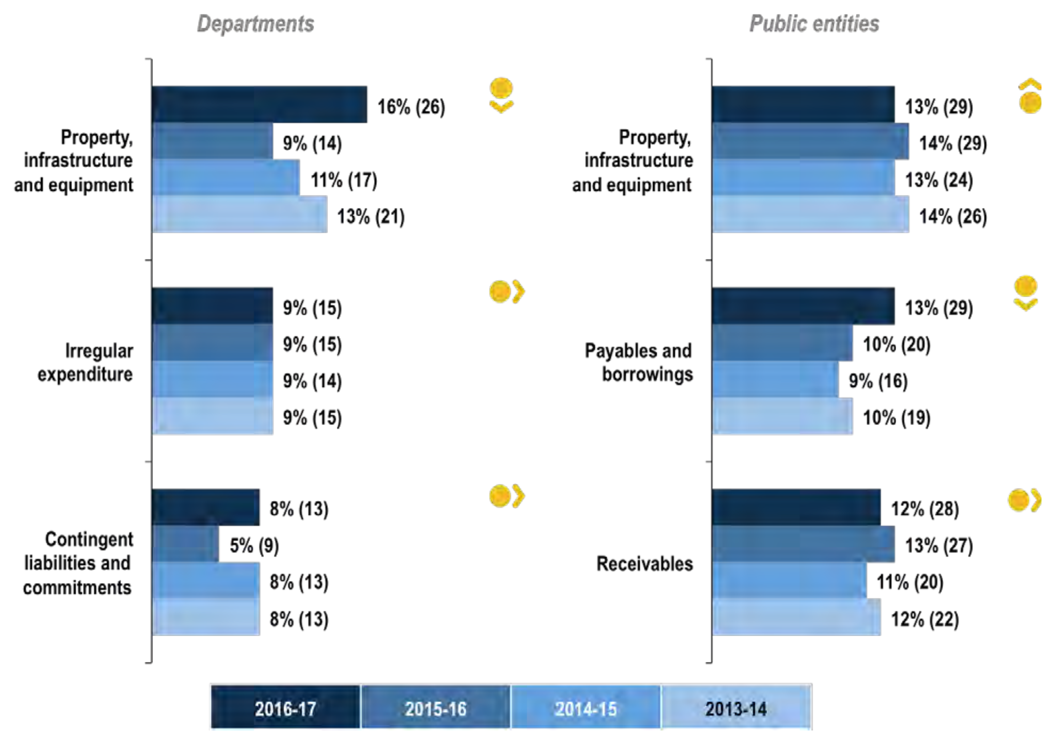
Portfolio	Financially unqualified auditees before correction of material misstatements		Financially unqualified auditees after correction of material misstatements	
	Number	Movement from 2015-16	Number	Movement from 2015-16
National auditees	125 (57%)	↑	173 (78%)	↓
Eastern Cape	13 (62%)	→	20 (95%)	→
Free State	6 (38%)	↑	9 (56%)	↑
Gauteng	15 (65%)	→	23 (100%)	→
KwaZulu-Natal	12 (52%)	↓	19 (83%)	→
Limpopo	3 (14%)	↓	13 (62%)	→
Mpumalanga	8 (47%)	↑	11 (65%)	→
Northern Cape	7 (54%)	→	11 (85%)	↓
North West	2 (9%)	↓	7 (32%)	↓
Western Cape	19 (100%)	→	19 (100%)	→
Total	210 (53%)	↑	305 (77%)	↓

The second column of table 1 indicates the low percentage of auditees in national and provincial government that would have received an unqualified audit opinion if no corrections had been made to the financial statements (in other words, those that submitted financial statements with no material misstatements). It also shows that there has been an improvement in the quality of submitted financial statements in the Free State and Mpumalanga but a regression in KwaZulu-Natal. North West and Limpopo had the poorest quality submissions with only two and three auditees, respectively, that could produce financial statements without material misstatements, whereas the Western Cape must be commended as the only province where 100% of the auditees could do so. Furthermore, the fourth column of table 1 shows that the national sphere, the Western Cape, Gauteng and the Eastern Cape had the most auditees that received financially unqualified audit opinions.

Although there has been a slight improvement, the status of submitted financial statements with no material misstatements remains concerning and points to a lack of implementation of basic financial disciplines, such as regular reviews of financial information during the year, a lack of in-year reporting, reliance on consultants to prepare financial statements at some auditees as well as reliance on auditors to identify errors in the financial statements. The 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. Over the years, this has placed undue pressure on the audit teams to meet legislated deadlines for the completion of audits, with an accompanying increase in audit fees.

Figure 5 shows the three most common financial statement qualification areas of departments and public entities whose financial statements received a modified opinion, and the progress made in addressing these areas since 2013-14.

Figure 5: Most common financial statement qualification areas



The number of auditees qualified in these areas had not changed significantly over the four years, or from the previous year, except for the 2016-17 **increase in departments qualified on property, infrastructure and equipment.**

The main reason for auditees being qualified on property, infrastructure and equipment was that the value of assets recorded in the financial statements was incorrect or we could not confirm the value at which these assets had been recorded. Thirteen departments were also qualified in the previous year and eight since 2013-14, of which four are departments in Limpopo and three are health departments. Thirteen departments were also qualified on property, infrastructure and equipment for the first time in 2016-17. There were mainly two reasons for the increase:

- Departments have been accounting for the **value of buildings** that are being built or upgraded in an annexure to the financial statements since 2013-14. We did not audit the annexures as they were not part of the financial statements. The National Treasury announced in 2015 that these values would become part of the notes to the financial statements from 2016-17 and would thus be subject to auditing. We communicated to the departments that this is an emerging matter for which departments should prepare. However, departments did not establish the necessary processes to ensure that the values were correct, which led to the qualifications.
- Some departments use **implementing agents** to implement projects on their behalf; for example, to build infrastructure or provide support to farmers. The accounting for the infrastructure or other assets that are constructed or purchased through these relationships is dependent on the nature of the arrangements with the agents. We identified incorrect accounting of these 'principal-agent' transactions at a number of departments in 2015-16 and increased our focus on this in 2016-17, resulting in increased qualifications. We typically found that departments accounted for the payments to the agents as transfer payments even though the accounting standards state that for certain arrangements they should account for it as expenditure and recognise the assets.

Overall, 17 (59%) of the 29 public entities qualified were TVET colleges. We found that the systems, skills and processes required to ensure correct accounting for assets were generally lacking at these colleges.

The main reason for departments being qualified on the **irregular expenditure** disclosed in their financial statements was that not all irregular expenditure had been disclosed, or sufficient evidence could not be obtained that all irregular expenditure had been disclosed. The qualifications were most common in the health, agriculture and education sectors.

Departments were qualified on **contingent liabilities and commitments**, as not all contingent liabilities and commitments had been disclosed in the financial statements or we could not obtain sufficient evidence that all had been included.

The main reason for public entities being qualified on **payables and borrowings** was that the value of payables disclosed in their financial statements was incorrect or we could not confirm the value at which payables had been recorded.

The main reason for public entities being qualified on **receivables** was that they had difficulty in accurately disclosing all amounts receivable in their financial statements or that they had calculated and recorded receivable amounts incorrectly. The qualifications were most common at the TVET colleges (21).

At the heart of the financial misstatements identified during our audits is auditees that failed to institutionalise internal control mechanisms that were mature and responsive enough to detect and prevent misstatements during the year and to correct these timeously. Furthermore, vacancies and a lack of financial management skills in finance units often had a significant impact on the quality of the financial statements – section 11 provides more information in this regard.

We recommend the following:

- Auditees should perform periodic, independent reconciliations between registers and records, including implementing processes to address errors or omissions.
- Auditees should implement detailed registers for project allocations and contracts approved / not yet approved to provide a reliable source for disclosures, such as commitments.
- Departments should re-assess the record keeping and reliability of reports used to value buildings. All departments that make transfer payments should also assess the relationship with the agent in terms of the 'principal-agent' standard.
- TVET colleges should provide employees in the finance units with adequate training to ensure that staff are kept updated on the changes in financial reporting requirements and the application thereof.
- Auditees should conduct detailed evaluations of the possible integration of IT systems that can be used to reduce manual registers.
- Internal audit units should be used to provide assurance on key areas of the financial statements – focusing on those that were misstated in previous years. Audit committees also need to intensify their review of the financial statements to prevent material misstatements in the versions submitted to us for auditing.

Conclusion

Sustainable improvements in financial management can be achieved if the leadership clearly defines the targets to be achieved in terms of audit outcomes, by using audit action plans (**PLAN**).

The basic disciplines of proper record keeping and standard daily and monthly controls built on a foundation of effective and efficient leadership and stability in key positions will enable a robust financial management system (**DO**).

Regular, credible in-year reporting monitored by, and acted upon, senior management and the accounting officer or authority as well as reports and recommendations on financial management and compliance from the internal audit unit and the audit committee will enable corrective action to be taken if targets are not achieved or if transgressions or poor performance is identified (**CHECK**).

Consistently investigating poor performance and applying consequence management will ensure that a culture of accountability prevails (**ACT**).

A

Annexure 1 available on our website provides detail on the quality of the financial statements of all auditees.

8 Performance reports

8. *Performance reports*

Performance reports are a key accountability mechanism. In the performance reports, auditees report on whether they achieved the objectives that had been determined in the planning and budgeting process, which include the delivery of projects and services to the benefit of citizens.

Figure 1 provides a four-year overview of our findings on the performance reports, the performance reports submitted with no material misstatements (orange line), and the auditees that did not submit performance reports or submitted them late. Table 1 provides the status of performance reports in national and provincial government.

Figure 1: Findings on performance reports and the quality and timeliness of submission for auditing

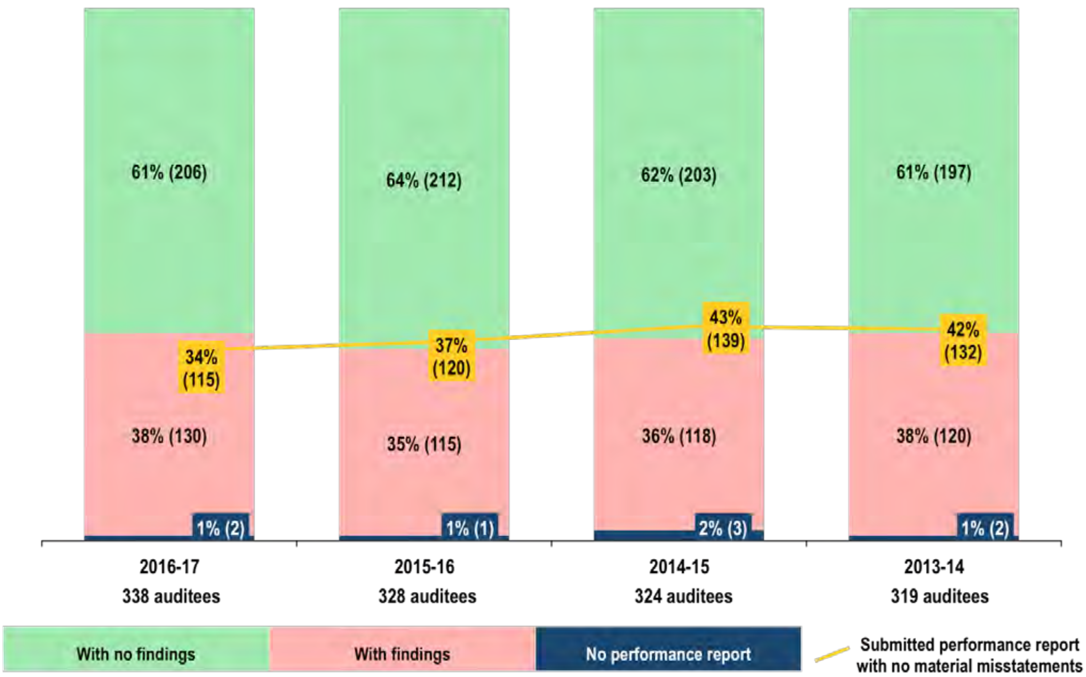


Table 1: Status of performance reports in national and provincial government

Portfolio	Auditees with no findings before correction of material misstatements		Auditees with no findings after correction of material misstatements	
	Number	Movement from 2015-16	Number	Movement from 2015-16
National auditees	38% (63)	↓	67% (112)	↑
Eastern Cape	38% (8)	↑	62% (13)	→
Free State	21% (3)	↓	29% (4)	↓
Gauteng	41% (9)	↓	77% (17)	↓
KwaZulu-Natal	23% (5)	↓	64% (14)	↓
Limpopo	29% (6)	↑	48% (10)	↓
Mpumalanga	29% (5)	↓	53% (9)	↓
Northern Cape	15% (2)	↓	69% (9)	↑
North West	5% (1)	→	10% (2)	↓
Western Cape	72% (13)	→	89% (16)	→
Total	34% (115)	↓	61% (206)	↓

As depicted in figure 1, there had been limited movement in the number of auditees with **no material findings** on the quality of their performance reports since 2013-14, with a slight regression since the previous year. The Free State, KwaZulu-Natal, Limpopo, Mpumalanga and North West regressed during 2016-17, with Gauteng slightly regressing.

The following auditees did not prepare performance reports:

- North West: The North West Tourism Board did not prepare a report this year, as it is the first year that they had to prepare a performance report and no official was appointed to take responsibility for submitting a performance report.
- National auditees: The Courier and Freight Group (a subsidiary of Sapo) failed to prepare a report in the current and previous year because they had no corporate plan or shareholders compact, and the indicators and targets included in the Sapo planning or reporting documents were insufficient.

Overall, 166 auditees had no material findings in the current and previous year, which means that the controls and processes required to produce credible performance reports were in place to sustain the quality of these reports.

Figure 1 also shows a reduction since 2013-14 and a slight regression from the previous year in the number of auditees that submitted performance reports that contained no material misstatements. In total, 91 auditees (27%) had no material findings on the quality of their performance reports in their 2016-17 audit report only because they corrected all the misstatements we had identified during the audit.

The fourth column of table 1 shows the combined number of auditees that submitted performance reports with no material misstatements as well as those that had corrected the material misstatements. There was an improvement in the Northern Cape with a slight improvement at national auditees, while the Free State and North West had the lowest number of auditees with no material findings on their performance reports after correction. High numbers of auditees with no material findings were most noticeable in the Western Cape, Gauteng and the Northern Cape.

Figure 2 reflects the findings on the usefulness and reliability of performance reports over the four years for all auditees that had prepared and timeously submitted performance reports. Figures 3 and 4 look at the status in this regard at departments and public entities, respectively.

Figure 2: Findings on the performance reports prepared

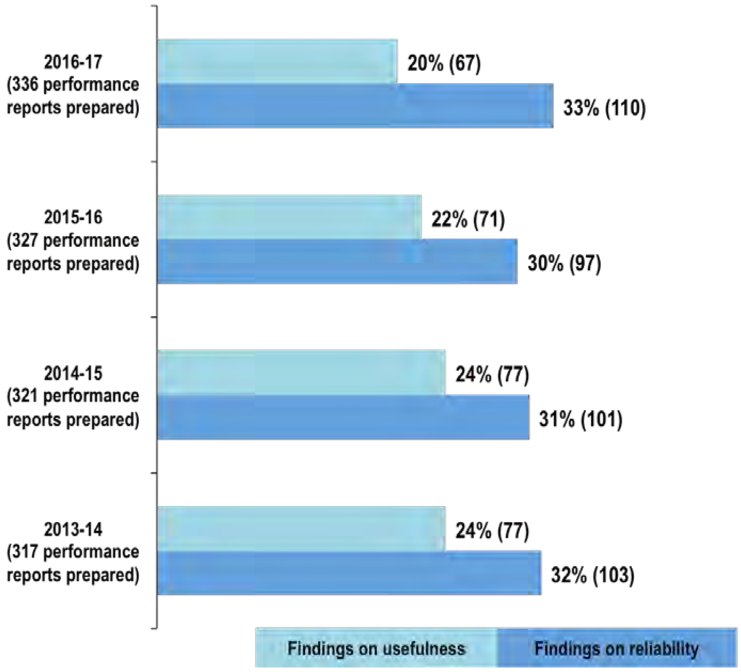


Figure 3: Findings on performance reports and quality and timeliness of submission for auditing – departments

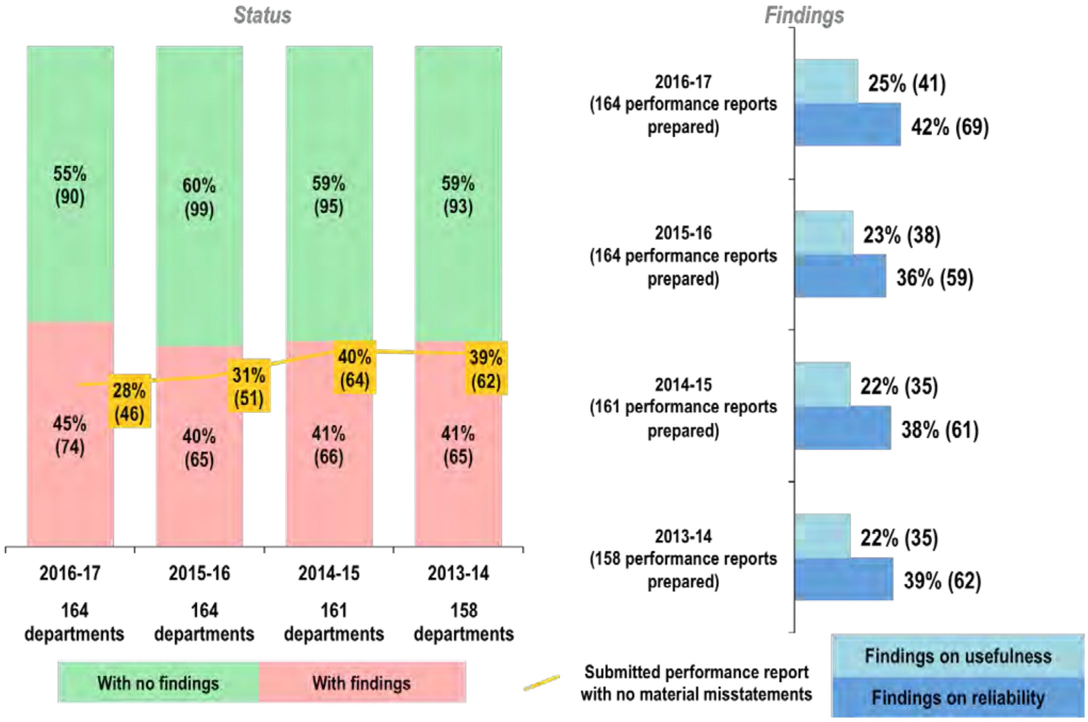


Figure 4: Findings on performance reports and quality and timeliness of submission for auditing – public entities

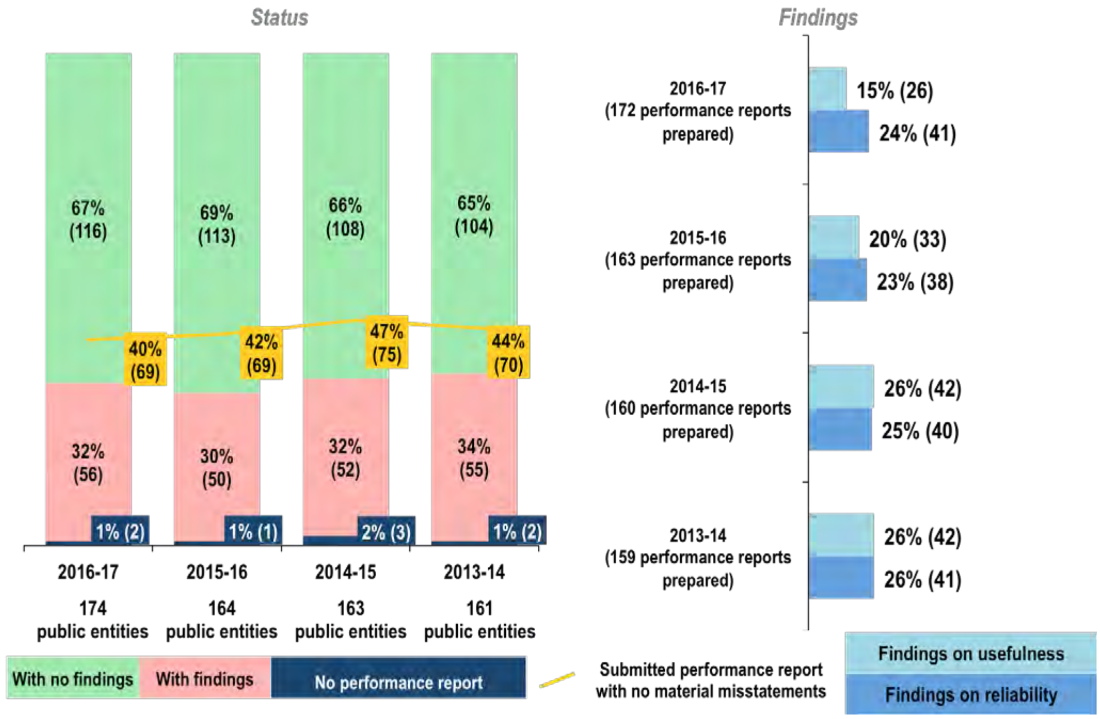


Figure 3 shows a slight regression at departments since 2013-14 and from the previous year. The number of public entities with no material findings increased (the percentage shows a regression, but it is as a result of a significant increase in the number of auditees being audited since 2013-14). The material findings have remained high in the education, health and public works sectors at 70% (21 of 30 auditees) – an improvement from the previous year.

As can be seen in figure 2, there had been a slight overall improvement in the **usefulness** of the information in the performance reports since 2013-14 and from the previous year. However, departments showed a slight regression over the four-year period and since 2015-16. The regression was notable in the Eastern Cape and the Northern Cape, while North West had the highest number of departments with findings on usefulness (77%).

The most common findings on usefulness in 2016-17 were that auditees reported on indicators that were not well defined (12%) or verifiable (6%); and targets were not measurable (7%) or specific enough (6%) to ensure that the required performance could be measured and reported in a useful manner.

The usefulness of the reported information continued to improve, as auditees corrected their performance indicators and targets as part of the annual planning and budget processes based on our recommendations and their increased understanding of the application of the requirements for performance planning.

Figure 2 also shows that there had been an increase in the number of auditees with findings on the **reliability** of their performance reports since 2013-14. The increase was as a result of a slight regression in the reliability of the performance reports of departments. All the **health** departments (with a combined budget of R164 billion) had findings on reliability during 2016-17, while eight **education** departments had findings in this area.

The prevalence of performance reports containing information that is not reliable or useful is a sign of serious weaknesses in the ability of auditees to adequately plan, manage and report on their performance. Accounting officers and authorities have a responsibility to set targets that are aligned to the government priorities defined in the MTSF and to account for the achievement thereof.

We therefore recommend the following:

- Auditees should integrate performance reporting into the regular financial reporting routines. This will ensure that there are sufficient controls to address the gaps created by treating performance reporting as an isolated event rather than a process linked to financial reporting.
- Auditees should collaborate with other sectors to implement and improve adequate computerised systems for identifying, collecting, collating, verifying and storing information; and move away from manual processes.
- Internal audit units and audit committees need to be better utilised for independent reviews of the information reported.
- Targets should be intensively reviewed to ensure that there are adequate available resources that are under the control of the auditee, and that targets are achievable within the set time frames and financial constraints.
- In addition to aligning service delivery requirements to reporting systems, the leadership should evaluate the potential financial impact of performance information that is not useful or reliable.

Conclusion

Sustainable improvements in performance management and service delivery can be achieved if the leadership clearly defines the targets to be achieved by using, among other, the strategic plan, annual performance plans and the annual budget (**PLAN**).

The basic disciplines of proper record keeping and standard daily and monthly controls built on a foundation of effective and efficient leadership and stability in key positions will enable a robust performance management system (**DO**).

Regular, credible in-year reporting monitored by, and acted upon, senior management, the accounting officer or authority, executive authorities as well as reports and recommendations on performance management from the internal audit unit and the audit committee will enable corrective action to be taken if targets are not achieved (**CHECK**).

Consistently investigating indicators of poor performance and applying consequence management will ensure that a culture of accountability prevails (**ACT**).

These improvements in performance management will enable better audit results, but more importantly contribute to a better life for all citizens (**IMPACT**).

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Annexure 1 available on our website lists the auditees with findings on their performance reports (predetermined objectives).

9 Compliance with key legislation

9. *Compliance with key legislation*

Figure 1 depicts the number of auditees that had material findings on compliance over the past four years, while table 1 indicates the status of compliance in national and provincial government at the auditees whose audits had been completed.

Figure 1: Auditees with findings on compliance with key legislation

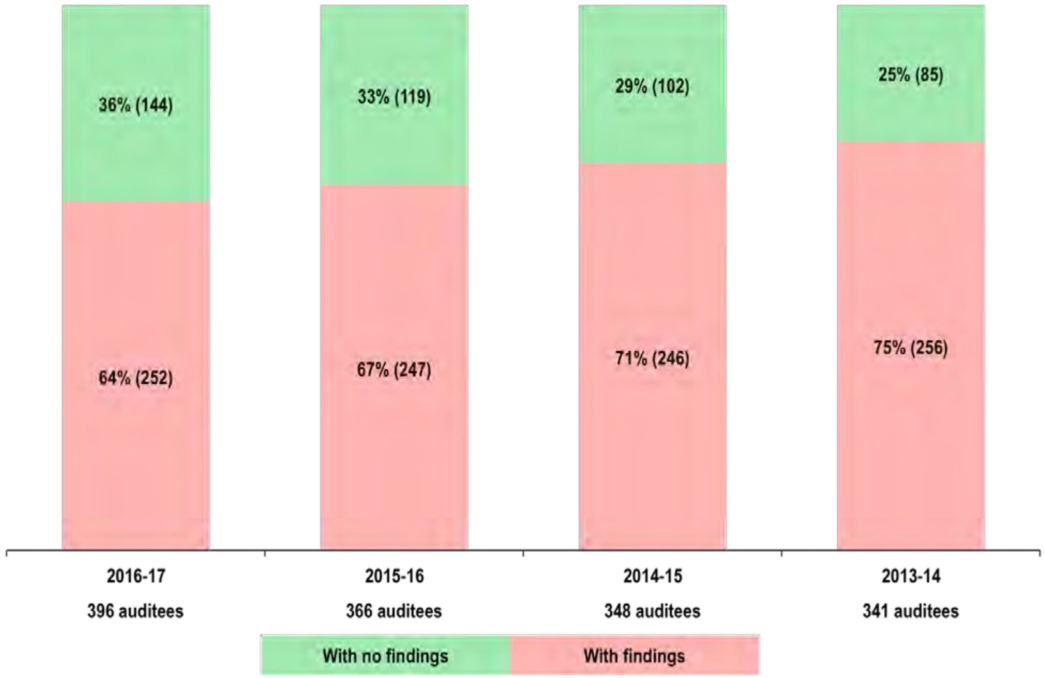


Table 1: Status of compliance with key legislation in national and provincial government

Portfolio	Auditees with no findings on compliance	
	Number	Movement from 2015-16
National auditees	86 (39%)	
Eastern Cape	7 (33%)	
Free State	3 (19%)	
Gauteng	12 (52%)	
KwaZulu-Natal	4 (17%)	
Limpopo	2 (10%)	
Mpumalanga	5 (29%)	
Northern Cape	4 (31%)	
North West	2 (9%)	
Western Cape	19 (100%)	
Total	144 (36%)	

With regard to the completed audits, the percentage of auditees **with material findings had decreased** over the four-year period with a further slight decrease since the previous year from 67% to 64%. The compliance outcomes for the provinces remained relatively unchanged, with Limpopo and the Free State improving on the number of their auditees with no compliance findings.

Figures 2 and 3 show the status and compliance areas with the most material findings over the four years at departments and public entities, respectively.

Figure 2: Status of compliance in most common areas of non-compliance – departments

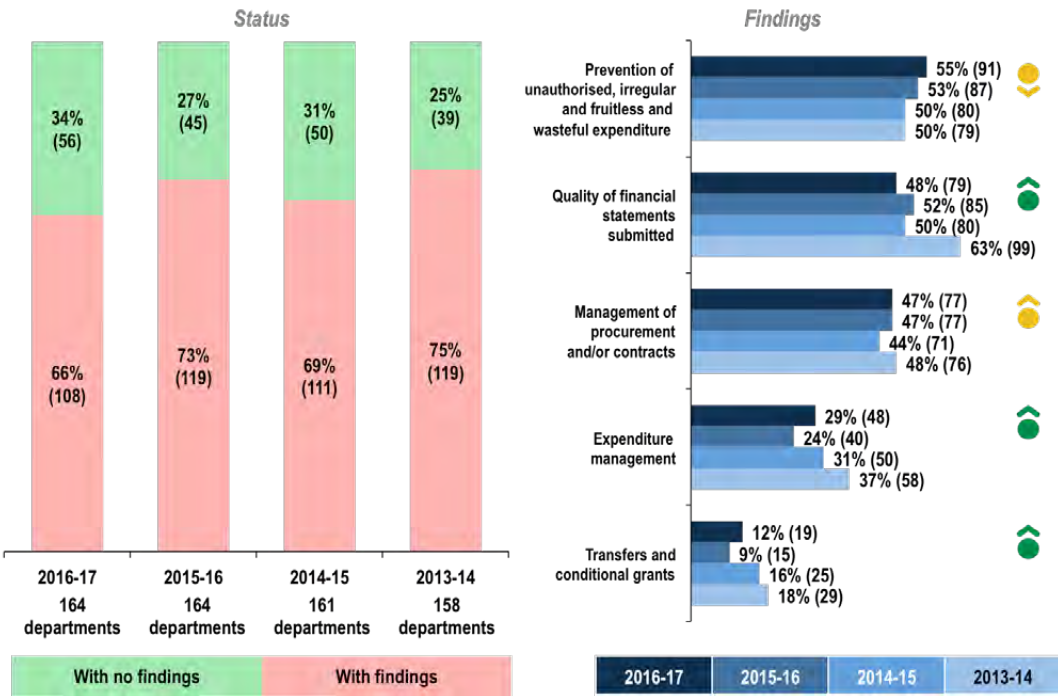
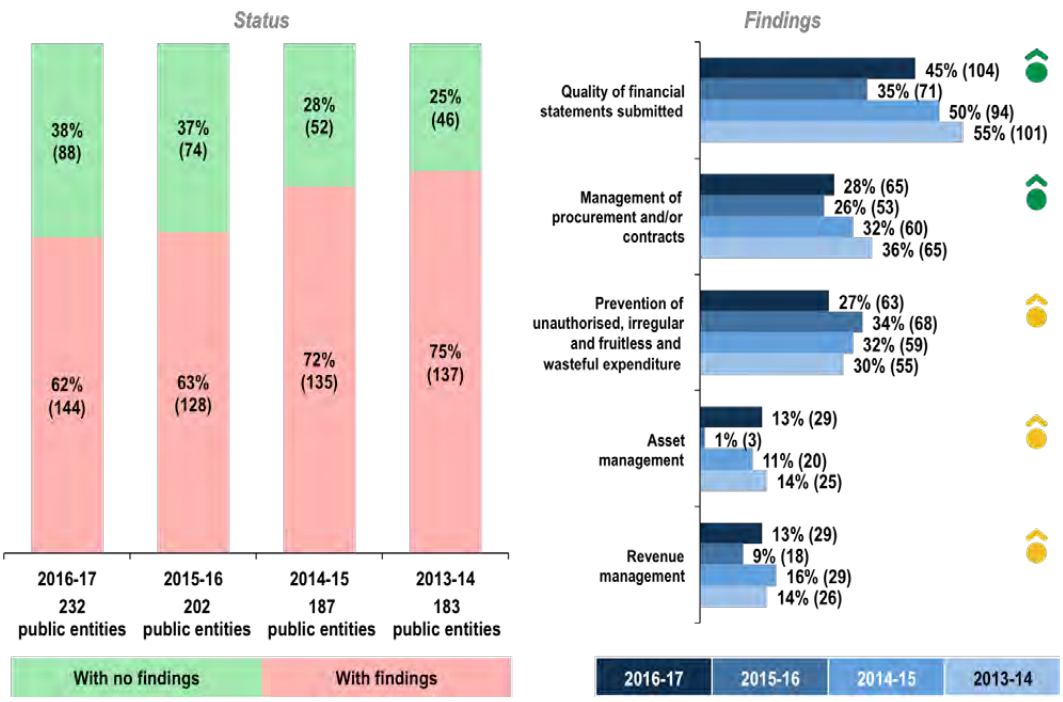


Figure 3: Status of compliance in most common areas of non-compliance – public entities

(As the number of public entities we report on increased significantly over the four years, the movement arrows in the graphic are based on the number of public entities with findings and not the percentage)



As shown in figure 2, the **compliance by departments had improved** since 2013-14 and the previous year but remained high with two-thirds of departments materially not complying with legislation. Countrywide, 87% of the departments of **education, health and public works** had findings on compliance with key legislation. This remained relatively unchanged from the previous year when 90% of these departments had findings. Limpopo and KwaZulu-Natal had the highest number of departments with compliance findings at 92% and 87%, respectively.

Figure 3 shows that the **number of public entities with material findings had increased** since 2013-14 and the previous year (the percentage shows an improvement, but it is as a result of a significant increase in the number of auditees being audited since 2013-14).

Our audits in 2016-17 did not include an assessment of the financial impact of the non-compliance by auditees. Based on the nature of the compliance findings, however, we determined that 175 (69%) of the auditees with material findings on compliance in 2016-17 had **findings with a potential negative financial impact or findings that could cause a financial loss** for the public entity or government. It is the role of those charged with governance to investigate non-compliance and the impact thereof, which could include financial loss through excessive expenditure (uneconomical use of funds), fruitless and wasteful expenditure, lost revenue, failure to recover debt, and avoidable penalties and interest.

There had been a slight regression in the **prevention of unauthorised, irregular and fruitless and wasteful expenditure** at departments since 2013-14 and the previous year as indicated in figure 2, while figure 3 shows that the number of public entities that did not comply in this regard had increased since 2013-14 although there was a slight improvement from the previous year. Sections 5, 9.1 and 9.2 provide more information on the movements in these areas.

We report the poor quality of the financial statements we receive in the audit reports of some auditees as a material finding on compliance, as it also constitutes non-compliance with the PFMA. The finding is only reported if the financial statements we received for auditing included **material misstatements** that could have been prevented or detected if the auditee had an effective internal control system. We do not report a finding if the misstatement resulted from an isolated incident or if it relates to the disclosure of unauthorised, irregular or fruitless and wasteful expenditure identified after the financial statements had been submitted. Section 7 provides more information on the movements in this area.

There had been little change since 2013-14 in the number of material findings on compliance with legislation in respect of **procurement and contract management** (also referred to as SCM) at departments, with no change since the previous year. Public entities also showed little improvement. Section 9.1 provides more information on the findings and movements in this area.

While there was an improvement from 2013-14, departments continued to struggle with **expenditure management**. In 2016-17, 26% of departments did not pay creditors within 30 days or an agreed-upon period – a regression when compared to the 21% in the previous year. We provide more information in section 5 on financial health and the state of payments within 30 days across all auditees.

The most common finding at departments on **transfers and conditional grants** was that appropriate measures had not been taken to ensure that receiving entities applied transfers for their intended purposes. There had been an improvement in this area over the past four years, although there had been a slight regression from the previous year. Section 3 includes information on the use of grants for some of the programmes – also refer to section 16 for our findings at a provincial level.

There was an increase in the number of public entities with findings on **asset management**. The main finding was that proper control systems had not been implemented to safeguard and maintain assets.

Effective and appropriate steps were not taken to collect all money due. This remained a common finding under **revenue management** at public entities, with little improvement in this area since 2013-14.

In addition to the most common areas of non-compliance in figures 2 and 3, we also raised findings in the following areas:

- Consequence management – 31 auditees (2015-16: 31) (refer to section 9.3 for more information in this regard)
- Management of strategic planning and performance – 19 auditees (2015-16: 29)
- Timing and/or content of financial statements and annual reports – 15 auditees (2015-16: 38)
- Preparation and/or control of budgets – 13 auditees (2015-16: seven)

9.1 Irregular expenditure caused by weaknesses in supply chain management

9.1 Irregular expenditure caused by weaknesses in supply chain management

What is irregular expenditure?

Irregular expenditure is expenditure that was **not incurred in the manner prescribed by legislation**; in other words, somewhere in the process that led to the expenditure, the auditee did not comply with the applicable legislation.

Such expenditure does **not necessarily mean that money had been wasted or that fraud had been committed**. It is an indicator of non-compliance in the process that needs to be investigated by management to determine whether it was an unintended error, negligence or done with the intention to work against the requirements of legislation. Such legislation requires, for example, that procurement should be fair, equitable, transparent, competitive and cost-effective.

Through such **investigation**, it is also determined who is responsible for the non-compliance and what its impact was. Based on the investigation, the next steps are determined. One of the steps can be condonement if the non-compliance had no impact and negligence was not proven. Alternatively, if negligence was proven, the steps can be disciplinary action, recovery of any losses from the implicated officials or even cancelling a contract or reporting it to the police or an investigating authority.

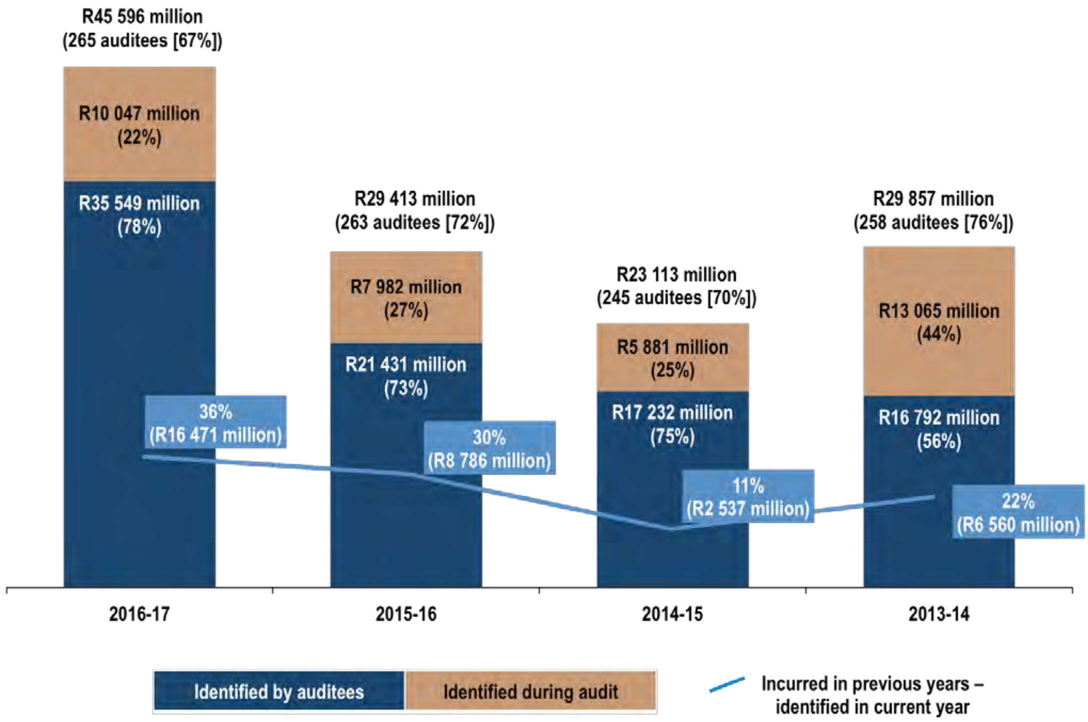
The PFMA is clear that **accounting officers and authorities are responsible** for preventing irregular expenditure. It also stipulates the process to be followed when it does occur, as described above.

In order to promote transparency and accountability, auditees **must disclose all irregular expenditure identified (whether by the auditee or through the audit process)** in their financial statements together with details on how it was resolved; in other words, how much was investigated, recovered or condoned.

Status of irregular expenditure

Figure 1 shows the four-year trend in irregular expenditure based on the amounts disclosed in the financial statements of auditees. It also indicates the percentage of irregular expenditure identified by auditees versus that identified by the audit process as well as the proportion of irregular expenditure disclosed that had been incurred in previous years (blue line).

Figure 1: Four-year trend in irregular expenditure
(excludes outstanding audits, such as that of Prasa)



As can be seen in figure 1, **irregular expenditure had increased by 55%** (R16 183 million) from the previous year and by 53% (R15 739 million) from 2013-14. The number of auditees incurring such expenditure had increased to 265. A total of 229 (86%) of these 265 auditees had **also incurred irregular expenditure in the previous year,** of which 177 (67%) had incurred such expenditure for the past four years. **The total irregular expenditure incurred over the past four years** was R128 billion.

The **total irregular expenditure for 2016-17 is even higher** than the R45 596 million shown in figure 1, as the irregular expenditure disclosed by auditees whose audits had been completed before the date of this report (but was not included in the analysis) was R1 091 million. The auditees of which the audits had not been completed also typically incur high irregular expenditure; for example, Prasa disclosed irregular expenditure of R13 971 million in 2015-16. Section 6.2 provides more information on these outstanding audits.

Auditees in KwaZulu-Natal, the Free State, Limpopo and the Eastern Cape were the **main contributors to the significant increase in irregular expenditure from the previous year** as indicated below:

- KwaZulu-Natal – R7 781 million (increased by 218%) (also had the highest amount of irregular expenditure in 2016-17)
- Free State – R3 494 million (increased by 181%)
- Limpopo – R1 545 million (increased by 150%)
- Eastern Cape – R1 136 million (increased by 92%)

The **sectors** with the highest amounts of irregular expenditure were health (R11 777 million), transport (R6 378 million) and education (R6 090 million).

Figure 1 further shows that 64% of the irregular expenditure was as a result of non-compliance in the current year, but that 36% was the result of **acts of non-compliance in previous years**. This is typically due to one of the following scenarios:

1. Payments were made in the current year on a contract that had been irregularly awarded in a previous year – if the non-compliance was not investigated and condoned, the payments on these multi-year contracts will continue to be viewed and disclosed as irregular expenditure.

2. Non-compliance in previous years was only identified in the current year and all the related expenditure (even from the previous years) was disclosed in the current year.

If we determine that an auditee did not fully disclose all of its irregular expenditure in the financial statements, the disclosure is qualified if material. To address such a qualification, auditees typically do a very detailed review of their processes in previous years to identify all the irregular expenditure and correctly disclose it – as per scenario 1 above. In total, R7 562 million (2015-16: R546 million) of the irregular expenditure as shown in figure 1 was as a result of **auditees fully recognising their previous years' irregularities to address these qualifications**. It is encouraging that the full disclosure of irregular expenditure is being addressed, as it improves transparency and accountability.

As detailed earlier on in this section, inadequate action taken by accounting officers and authorities to **prevent irregular expenditure** was one of the most common material findings on compliance. We reported the findings on compliance as material at 89 departments (54%) (2015-16: 86 [52%]) and 60 public entities (26%) (2015-16: 65 [32%]), based on the fact that they incurred irregular expenditure in 2016-17 and the previous year, a recurrence of the transgressions that had caused such expenditure, and our assessment that adequate controls and processes would have prevented it.

Figure 1 also shows that we had identified 22% of the irregular expenditure of 2016-17 during the audit process (a slight improvement from the previous year), which means that some auditees **did not have adequate processes to detect and quantify all irregular expenditure**.

Completeness of irregular expenditure

In 2016-17, 98 auditees (25%) disclosed in their financial statements that they had incurred irregular expenditure, but the **full amount was not known** as it was still being investigated. In 2015-16, 88 auditees (24%) had made this disclosure.

A total of 28 auditees (7%) (2015-16: 29 [8%]) were qualified on the **completeness of the disclosure** of irregular expenditure in their financial statements, both in 2016-17 and 2015-16.

This means that the amount of irregular expenditure for 2016-17 **could have been higher** if the full amounts had been known and disclosed.

What caused these high levels of irregular expenditure?

As part of our audits of SCM in 2016-17, we tested 5 816 contracts (with an approximate value of R119 828 million) and 14 261 quotations (with an approximate value of R2 832 million), referred to as 'awards' in the rest of this report. Refer to section 17 for a description of the scope of our SCM audits.

Although not all non-compliance with SCM legislation results in irregular expenditure, the **high occurrence of irregular expenditure usually correlates with poor SCM practices**. There were slightly more auditees with SCM findings (282) than irregular expenditure in 2016-17, as – typically – SCM findings such as inadequate measures to monitor the performance of contractors would not result in irregular expenditure.

In total, R40 434 million (89%) (2015-16: 89%, R26 079 million) **of the irregular expenditure in 2016-17 was as a result of non-compliance with SCM legislation**. The following were the main areas of SCM non-compliance as disclosed by the auditees in their financial statements, with an indication of the estimated value of such expenditure:

- Procurement without a competitive bidding or quotation process – R14 958 million (37%) (2015-16: 43%, R11 259 million)
- Non-compliance with procurement process requirements – R21 489 million (53%) (2015-16: 50%, R12 968 million)
- Non-compliance with legislation relating to contract management – R3 987 million (10%) (2015-16: 7%, R1 852 million)

(We discuss the typical findings in these areas later on in this section.)

The **significant increase** in irregular expenditure from the previous year can be attributed to the auditees reporting on irregular expenditure to address prior year qualifications, poor consequence management, and inappropriate discretion by management (meaning that the accounting officers used their discretion to appoint targeted suppliers without following a competitive bidding process).

Table 1 shows the auditees that were the **main contributors (53%) to irregular expenditure in 2016-17**. The corresponding figures for 2015-16 are shown in *italics*.

Table 1: Highest contributors to irregular expenditure

Auditee	Amount (million)	Nature
Transport (KZN)	R3 952 *(2015-16: R477)*	A significant amount of the irregular expenditure related to a plant-hire contract for which the preference point system had not been applied. In some instances, deviations were approved even though it was not impractical to go through the competitive bidding process. Of this amount, R2 625 million related to prior years as an exercise was conducted to identify irregular expenditure from prior years. Of the R1 327 million relating to the current year, 55% (R727 million) related to plant hire while 23% (R307 million) related to the inappropriate deviation from procurement processes. Some of the payments for plant hire related to provincial roads maintenance grants.
Health (FS)	R3 502 *(2015-16: R466)*	Of the R3 502 million, R3 201 million (91,4%) was irregular expenditure identified to resolve prior year qualifications, while the remaining R301 million related to current year irregular expenditure. Procurement processes were incorrectly applied, as preference points were incorrectly calculated. In some instances, suppliers were incorrectly disqualified and functionality was not correctly determined. Some of these amounts related to money not spent in terms of conditional grants.
Health (KZN)	R3 025 *(2015-16: R2 521)*	Of this expenditure, R31 million related to the purchase of mobile units to be used for male circumcision. The full amount was funded from the HIV/Aids conditional grant. Most of this amount related to the prior year (i.e. R1 700 million). Included in this amount was R50,3 million paid to the Independent Development Trust, which acted as the implementing agent.
Human Settlements (KZN)	R2 888 *(2015-16: R6)*	Most of this amount related to the prior year (i.e. R2 328 million). Of the R560 million relating to the current year, almost 100% related to non-compliance with SCM legislation by municipalities regarding implementing agents on housing projects. Some of the irregular expenditure related to the human settlements development grant.
Roads and Transport (GP)	R2 380 *(2015-16: R2 032)*	The expenditure resulted from deviations from the competitive bidding process, R2 341 million (98%) of which related to the extension of a bus subsidy.
Health (GP)	R2 051 *(2015-16: R828)*	Of this expenditure, R597 million related to the extension or modification of contracts without appropriate approval while R491 million related to the procurement of construction contracts, security services as well as various contracts. Overall, 35% (R725 million) related to the payment of employee cost, as the budget for the compensation of employee cost was increased without approval by the provincial treasury.

Auditee	Amount (million)	Nature
Education (EC)	R1 873 *(2015-16: R265)*	The expenditure resulted from non-compliance across all SCM requirements, deviations from the SCM process as well as non-compliance with PFMA requirements when making transfers and paying subsidies. Most of this expenditure related to the prior year. Of the R784 million relating to the current year, 64% (R468 million) related to infrastructure.
Department of Water and Sanitation	R1 686 *(2015-16: R1 711)*	A total of R915 million of this expenditure related to non-compliance with SCM legislation by the implementing agent while R431 million related to the regional bulk infrastructure grant, water service infrastructure grant and sanitation contracts. Of this expenditure, R214 million was incurred on the supply, delivery and installation of a desalination plant for the drought-stricken Richards Bay.
Health (MP)	R1 642 *(2015-16: R1 920)*	The incorrect application of procurement processes, as preference points were incorrectly calculated in the prior year on a medical supplies contract, accounted for 94% of the irregular expenditure. A total of 4% of the irregular expenditure related to non-compliance on the implementing agents' contracts and 2% to the department's own SCM processes. Overall, 16% (R267 million) of the total irregular expenditure related to conditional grants.
Roads Agency Limpopo (LP)	R1 195 *(2015-16: R49)*	A total of 89% (R1 060 million) related to non-compliance with legislation that was identified in the current year relating to the prior year. The entity investigated and quantified the full extent of the non-compliance and adequately disclosed this amount in the year under review.

These auditees are among those that had **incurred irregular expenditure for the past four years**. As apparent from table 1, most of the irregular expenditure of the top 10 contributors related to prior years, pointing to auditees performing detailed reviews to address prior year qualifications on irregular expenditure in some instances. We are concerned about the irregular spending of grant money by six of the top 10 contributors.

Implementing agents are increasingly being used to manage and implement projects on behalf of departments. The agents can be government institutions (e.g. the Independent Development Trust), non-governmental organisations or private sector entities. As can be seen in table 1, this was the cause of irregular expenditure by four of the top 10 contributors, Section 3 details findings relating to the management and delivery of key programmes (which include findings on selected grants and implementing agents).

We did not investigate the irregular expenditure, as that is the role of the accounting officer or authority. Through our normal audits, however, we confirmed that **goods and services were received** for R24 609 million (61%) of the R40 434 million in irregular expenditure relating to SCM non-compliance, despite the normal processes governing procurement not having been followed. However, we could not confirm that these goods and services had been procured at the best price and that value was received for the money spent. Our normal audits also confirmed that **goods and services were not received for** R123 million (<1%) of the R40 434 million in irregular expenditure relating to SCM non-compliance. We did not audit the remaining 38%.

Section 9.3 provides our findings on the poor investigation and follow-up of irregular expenditure and outlines recommendations to improve these processes.

Supply chain management

We have been auditing and reporting on weaknesses in SCM for a number of years and our messages have been consistent on the need to pay urgent and focused attention to improving the SCM processes.

Figure 2 depicts the number of auditees that had SCM findings and those where we have reported material findings on compliance in the audit report since 2013-14.

Figure 3 shows the status of SCM findings at departments and public entities, while table 2 illustrates the progress made with regard to auditees with no findings on SCM.

Figure 2: Status of supply chain management

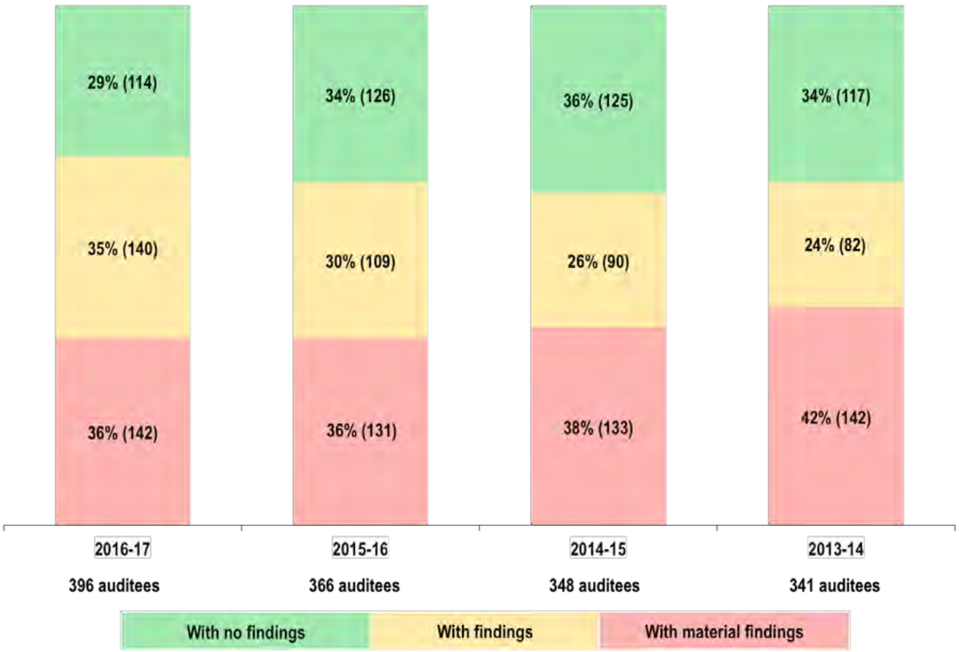


Figure 3: Status of supply chain management – departments and public entities

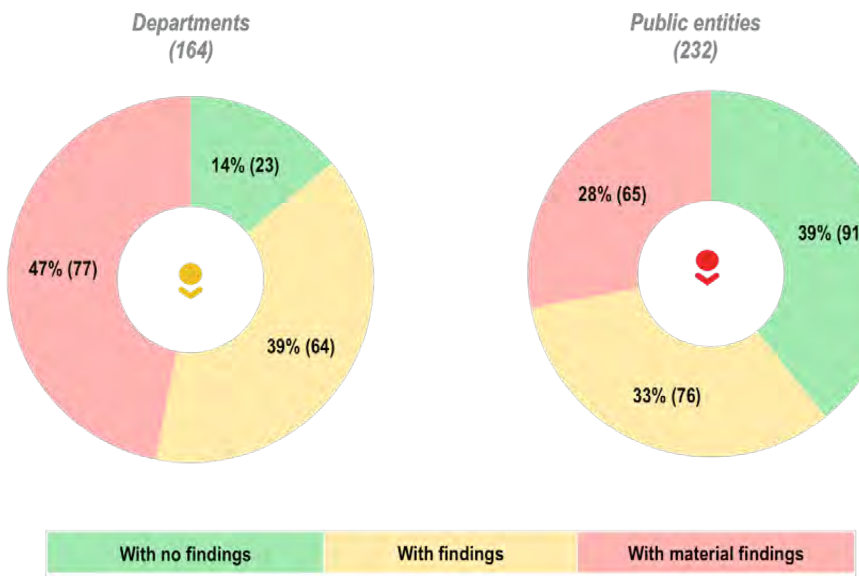


Table 2: Progress made with regard to supply chain management by national and provincial government

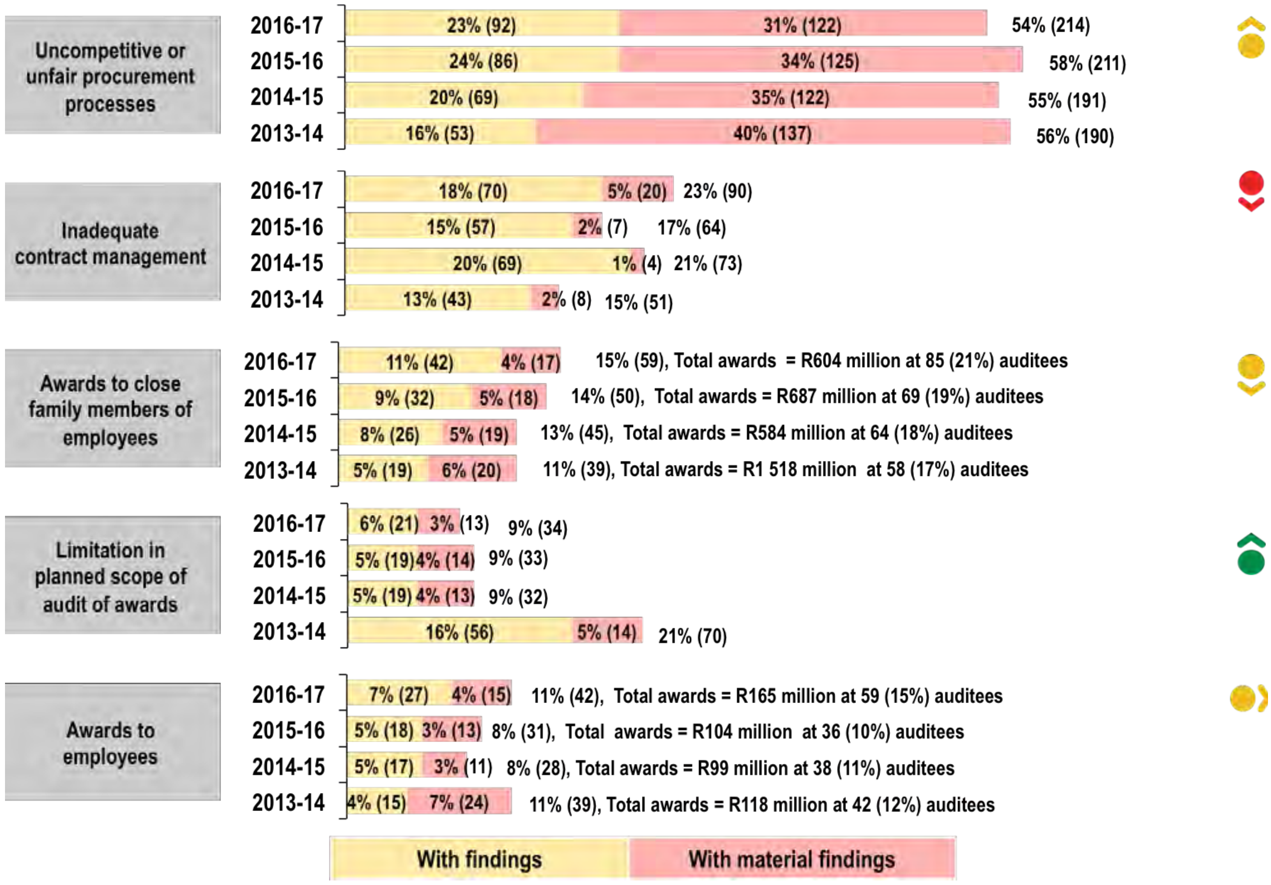
Portfolio	Auditees with no findings on supply chain management	
	Number	Movement from 2015-16
National auditees	76 (34%)	
Eastern Cape	4 (19%)	
Free State	1 (6%)	
Gauteng	10 (43%)	
KwaZulu-Natal	4 (17%)	
Limpopo	4 (19%)	
Mpumalanga	2 (12%)	
Northern Cape	1 (8%)	
North West	1 (5%)	
Western Cape	11 (58%)	
Total	114 (29%)	

Slightly fewer auditees than in the previous year had no SCM findings. There had also been a slight regression in auditees with no SCM findings since 2013-14. National auditees and those in the Free State and KwaZulu-Natal had regressed since the previous year, while those in Limpopo and Mpumalanga had improved. The provinces with the poorest SCM practices were the Northern Cape, North West and the Free State.

Although the percentage of auditees with material findings had improved since 2013-14, it remains concerning that almost half of the departments did not comply materially with SCM legislation in 2016-17. It is also of great concern that the number of public entities with no SCM findings had regressed since the previous year – from 50% to 39%. Although the SCM findings at 35% of the auditees were not material enough to be reported in the audit report, the control weaknesses that allowed the non-compliance to occur should be addressed to prevent a regression in audit outcomes in future.

Figure 4 provides a four-year overview of all the SCM areas in which auditees had findings, the number of auditees where the findings raised were material enough to be reported in the audit report, as well as the extent of awards made to employees and close family members of employees. The movement is shown over the four years.

Figure 4: Findings on supply chain management



The level of total SCM findings (material plus non-material findings) had shown little movement in any of the SCM areas since 2013-14, except for the regression in the area of contract management and a significant reduction in the number of auditees where we experienced limitations in our audits.

Limitation in planned scope of audit

In 2016-17, we were unable to audit awards to the value of R1 870 million at 34 auditees because the auditees **could not provide us with evidence that awards had been made in accordance with the requirements of SCM legislation**, as the documentation either did not exist or could not be retrieved as a result of poor document management.

Table 3 lists the extent of limitations in national and provincial government over four years.

Table 3: Extent of limitations on planned audits

Portfolio	2016-17 Number of auditees	2016-17 Amount R million	2015-16 Number of auditees	2015-16 Amount R million	2014-15 Number of auditees	2014-15 Amount R million	2013-14 Number of auditees	2013-14 Amount R million	Movement from 2015-16
National auditees	14	303	9	25	12	98	26	1 004	
Eastern Cape	2	2	2	357	0	0	8	68	
Free State	2	1	3	3	3	28	5	6	
Gauteng	2	56	3	183	1	6	4	10	
KwaZulu-Natal	3	929	3	1 239	4	51	4	10	
Limpopo	4	137	4	34	3	83	6	452	
Mpumalanga	0	0	3	17	5	345	4	19	
Northern Cape	3	405	1	81	1	137	4	9	
North West	4	37	5	587	3	536	8	515	
Western Cape	0	0	0	0	0	0	1	0	
Total	34	1 870	33	2 526	32	1 284	70	2 093	

While the number of auditees where limitations were experienced in 2016-17 had increased only slightly from the previous year, there was a more visible improvement in the Free State and Mpumalanga. The value of these limitations varied over the four years, as it depended on the value of the relevant contracts awarded in the year.

The auditees with the highest value of awards that we could not audit in 2016-17 were the following:

- Human Settlements (KwaZulu-Natal) – R894 million (2015-16: R1 220 million)
- Cooperative Governance, Human Settlements and Traditional Affairs (Northern Cape) – R360 million (2015-16: R80 million)
- SABC – R193 million (2015-16: amount undeterminable)
- Public Works, Roads and Infrastructure (Limpopo) – R94 million (2015-16: R0)
- Health (Gauteng) – R46 million (2015-16: R166 million)

These limitations had the following impact:

- The procurement processes could not be audited by us, the internal auditors or investigators.
- There was no evidence that auditees had followed a fair, transparent and competitive process for all awards. Should unsuccessful bidders request information on the process, also for possible litigation purposes, it would not be available.
- We could not determine whether these awards were irregular and, as a result, could not determine the true extent of irregular expenditure.
- Our general report, audit reports and management reports did not reflect the true extent of non-compliance with SCM, irregularities and possible fraud.
- Poor record management created an environment in which it was easy to commit and conceal improper or illegal conduct.

Awards to employees and close family members

As depicted in figure 4, awards to the value of R165 million (a total of 459 awards) were made to suppliers in which employees (including political office-bearers) had an interest at 59 auditees (15%) – a slight regression from the 36 auditees (10%) in the previous year. There had also been a slight regression since 2013-14. At five auditees (Mthashana TVET College, Umfolozi TVET College, Parliament of the Republic of South Africa, Northern Cape Provincial Legislature, and Wholesale and Retail Sector Education and Training Authority), awards were made to suppliers in which political office-bearers had an interest. Both directors and members of the accounting authority benefited from this undesirable practice at two auditees each. The value of these awards varied over the four years, as it depended on the value of the relevant contracts awarded in the year.

At 85 auditees (21%), awards to the value of R604 million (a total of 1 017 awards) were made to suppliers in which close family members of employees had an interest – a slight regression from the previous year as well as since 2013-14.

We identify suppliers in which employees or their close family members have an interest through basic data analysis. This analysis has its limitations; for example, we can only test registered companies and we do not have information on all family members, so it is likely that the extent of awards to employees and close family members could be even greater.

There had been little movement in the number of auditees **with findings on awards to suppliers in which employees or their close family members had an interest.** As auditees are not prohibited by current legislation to make such awards, the compliance findings we raised related to employees and suppliers not declaring their financial interests, including the following:

- Suppliers owned or managed by employees of auditees made **false declarations** in awards of R106 million at 12 auditees. Those owned by close family members of employees made false declarations in awards of R178 million at 34 auditees.
- In total, 16 **auditees did not request declarations of interest** as part of the procurement process as required by legislation and as a result did not identify that employees had an interest in awards of R10 million and close family members in awards of R111 million.
- At 31 auditees, **employees failed to declare their own interest** in awards of R54 million either as part of the procurement processes or through annual declarations. At 44 auditees, **employees failed to declare their family members' interest** in awards of R274 million.

These findings were most common in national government (27 auditees) and North West (nine auditees). The sectors that had the most of these findings were health (seven auditees) and education (six auditees).

The possibility of **undue influence** cannot be discounted, especially if the person, including SCM officials, could have influenced the procurement processes for these awards, which could have created opportunities for irregularities.

We again point out that a **failure by suppliers to declare the interest of employees constitutes a fraudulent act**, which should be investigated and dealt with in accordance with legislation. Section 9.3 provides more information on how auditees have dealt with this in the last four years.

Although there is no legislation that prohibits making awards to suppliers in which state officials have an interest, the **amended Public Service Regulations prohibit employees of departments from doing business with the state** from 1 August 2016. The regulations allowed employees that were doing business with the state on 1 August 2016 time until February 2017 to stop the business or resign as an employee.

In the first year of auditing this specific regulation, we found the following at 44 departments:

- Overall, 698 employees at 24 departments took **no action in this transitional period and continued doing business with the state**. Of these employees, 32 were doing business with the department that employs them (at five departments, awards to the value of R16 million were secured) and 666 were doing business with other organs of state (at 21 departments, awards to the value of R120 million were secured).

- In addition, 649 employees at 32 departments **secured new awards after 1 August 2016**, even though it is prohibited. Of these employees, 132 found new business with the department that employs them (at 15 departments, awards to the value of R18 million were secured) and 517 with other organs of state (at 23 departments, awards to the value of R108 million were secured).

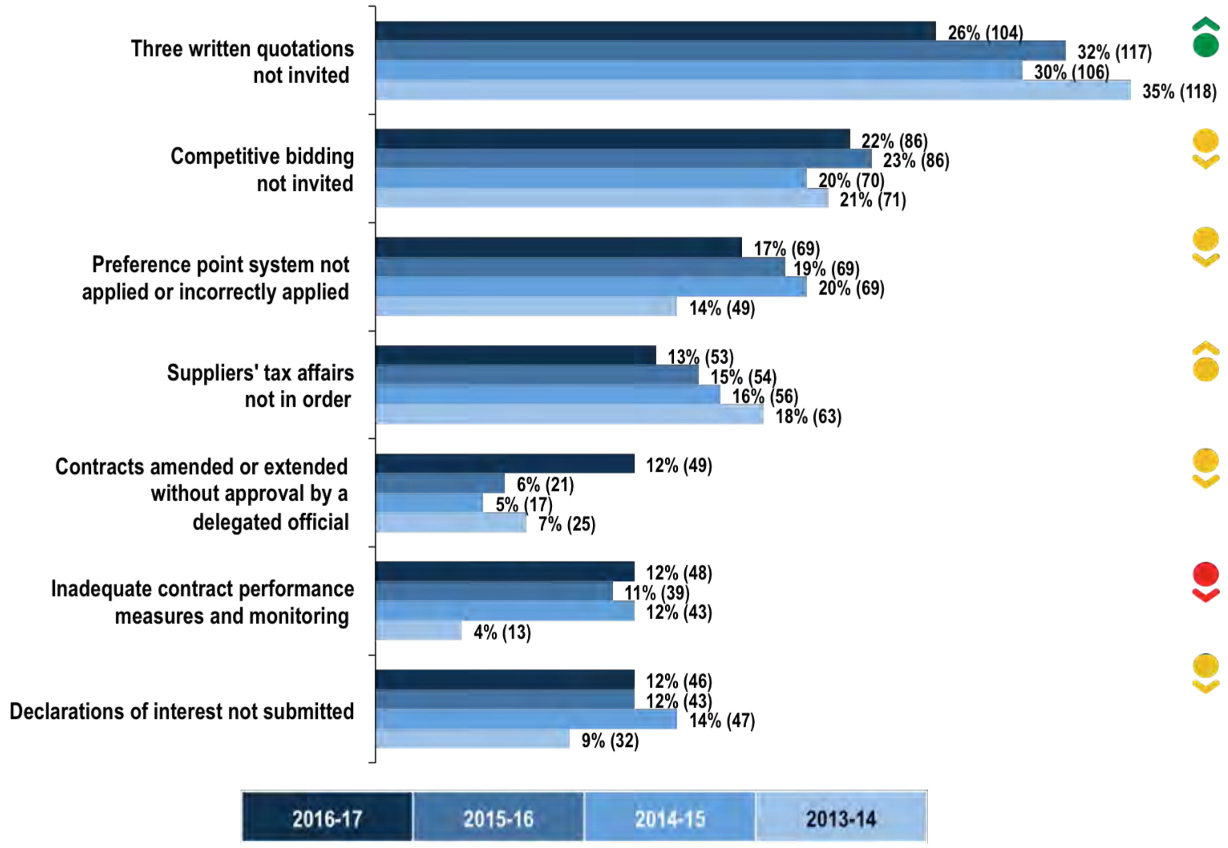
These findings were most common in national government (12 departments) and North West (eight departments). The sectors that had the most of these findings were education (seven auditees) and public works (three auditees).

The onus of complying with these regulations is on the employees of departments, but departments have a responsibility to enable and monitor such compliance. Based on the findings in just the first six months of implementation, it seems that this responsibility is not being given the attention it deserves.

Procurement processes and contract management

Figure 5 provides a four-year overview of the most common findings on procurement processes and contract management – all of which have a potential negative financial impact. All, except the findings on inadequate performance measures, lead to irregular expenditure. The movement is shown over four years.

Figure 5: Most common findings on procurement processes and contract management



The most common findings for the past four years related to **deviations from the prescribed procurement processes**. Three written quotations or competitive bids were not invited to enable the selection of a supplier based on a competitive and fair process. Although such deviations are allowed, we found that it had often not been approved; or, if approved, the deviation was not reasonable or justified. This points to the inappropriate use of management discretion in the procurement process. In some instances, the accounting officers used their discretion to appoint targeted suppliers without ensuring compliance with legislation.

The following are examples of such inappropriate discretion:

Public Works and Roads in North West deviated from the prescribed procurement processes and participated in a contract arranged by another organ of state, which is allowed by legislation. However, this contract was awarded by a municipality for its water programme, while the department used the consulting engineers for its road programme. The department also added a clause to the contract to use the consultant for any other work they may deem necessary and then awarded a further contract of R103 million to the same supplier in terms of this clause for the rehabilitation of flood-damaged roads. Payments were made on this contract without any service having been rendered by the date of payment.

The Department of Water and Sanitation appointed an implementing agent, as instructed by a ministerial directive, on a multi-year infrastructure project. The latter then proceeded to award a contract of R94 million without following proper procurement processes, stating the reason for the deviation as an emergency due to the unavailability of water and the drought experienced. However, subsequent to the initial emergency being addressed, this basis of emergency procurement continued to be utilised as a reason to add additional multi-year infrastructure projects, increasing the related projects to current expenditure of R2,2 billion, with future additional commitments of R10,8 billion. Had the additional projects been appropriately planned for, the emergency basis would not have been used to deviate from procurement processes.

In North West, the awards for various cluster security contracts were not made to the bidders recommended by the departmental bid adjudication committee. The accounting officer of Health deviated by appointing various other security companies that had not been recommended. His motivation was that preference should be given to local suppliers to be in line with the province's objective of VTSD (promoting business in villages, townships and small *dorpies*) and that some suppliers would not have the resources to provide services for all the clusters recommended by the bid adjudication committee. None of these reasons could be substantiated with evidence.

In the Eastern Cape, a printing tender of R125 million was awarded where the bid specifications were restricted through the inclusion of criteria related to the turnover and location of the printer, which effectively excluded all other printing companies that wanted to tender.

There had been an **improvement in the quotation processes** since the previous year and over the four-year period, which could be a sign of processes maturing and in particular as a result of the introduction of the central supplier database. However, the performance measures and monitoring of contracts are not showing improvement and we are concerned that the number of auditees where contracts were amended or extended without approval had doubled from the previous year. **Contract management is an area of poor control** that directly affects the delivery by the supplier and ultimately the success of government projects.

The Preferential Procurement Regulations make provision for the **promotion of local production and content.** These regulations are aimed at supporting socio-economic transformation. In 2015-16, we reported non-compliance with the regulations at 20 auditees and committed to increase our audit focus on this important government initiative. In 2016-17, we identified procurement in the designated sectors and **tested 91 contracts (with an approximate value of R1 068 million) and 1 788 quotations (with an approximate value of R99 million)** to determine whether it took place in accordance with the legislative requirements of procuring certain commodities from local producers.

Table 4 shows the extent of our findings in 2016-17.

Table 4: Local content findings

Portfolio	Total auditees where local content was tested	With findings	With material findings	Total local content findings
National auditees	38	9	9	18 (47%)
Eastern Cape	7	1	0	1 (14%)
Free State	2	1	0	1 (50%)
Gauteng	3	0	0	0 (0%)
KwaZulu-Natal	6	0	3	3 (50%)
Limpopo	7	3	1	4 (57%)
Mpumalanga	10	0	5	5 (50%)
Northern Cape	3	0	2	2 (67%)
North West	2	0	1	1 (50%)
Western Cape	13	4	0	4 (31%)
Total	91	18 (20%)	21 (23%)	39 (43%)

The 43% of auditees that did not comply with the requirements demonstrated a **lack of understanding and awareness** of the requirements and even a disregard for them, which could result in government not achieving the objectives of this initiative.

The SCM weaknesses require immediate and focused action to ensure that the principles of fairness, transparency, completeness, equity and cost-effectiveness in procurement processes are consistently applied, and to address the very high amounts of irregular expenditure incurred annually.

We propose the following recommendations to improve SCM, which will also reduce the irregular expenditure incurred:

- Strengthen the **SCM control environment** by appointing suitably skilled and qualified heads of SCM units where vacancies exist and conduct regular training to improve skills (**DO**).
- Focus on **preventing irregular expenditure and non-compliance** – this should be a key performance measure in senior officials' contracts (**DO**).
- Implement **SCM compliance checklists** to supplement policies and procedures (**DO**).
- Submit **regular reports** to management and governance structures on compliance with key legislation (**CHECK**).
- A **less tolerant approach** by all parties, including those charged with governance and oversight, will result in accountability and consequences being enforced against those who intentionally fail to comply with legislation (**CHECK**).
- Institute **corrective or disciplinary** action for misconduct (**ACT**).

A

On our website, annexure 1 shows the auditees that had incurred irregular expenditure, while annexure 2 lists those with findings on SCM.

9.2 Fruitless and wasteful expenditure

9.2 Fruitless and wasteful expenditure

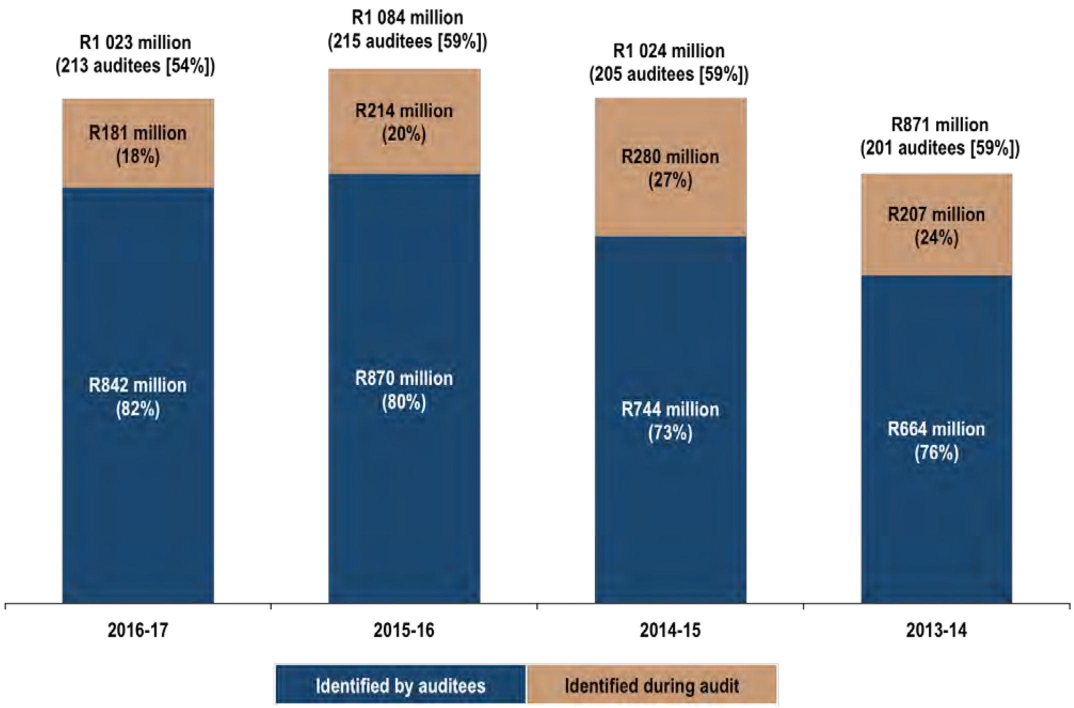
What is fruitless and wasteful expenditure?

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

Such expenditure includes interest, the payment of inflated prices, and the cost of litigation that could have been avoided.

Figure 1 depicts the extent of fruitless and wasteful expenditure over the past four years and the proportion thereof that was identified during the audit and not by the auditee.

Figure 1: Four-year trend in fruitless and wasteful expenditure



As shown in figure 1, the **amount of fruitless and wasteful expenditure** had increased by 17% since 2013-14 but decreased by 6% since the previous year. The number of auditees that incurred this type of expenditure had slightly decreased from 2015-16. Auditees in KwaZulu-Natal and Mpumalanga were the main contributors to the decrease in fruitless and wasteful expenditure from the previous year. The fruitless and wasteful expenditure in these provinces decreased by more than 80%.

A total of 176 auditees (83%) incurred fruitless and wasteful expenditure in both the current and the previous year, of which 129 had incurred such expenditure for the past four years.

The general **nature of the fruitless and wasteful expenditure** related to the following:

- Interest and penalties on overdue accounts and late payments – R369 million (36%) (2015-16: R149 million [14%])
- Litigation and claims – R141 million (14%) (2015-16: R588 million [54%])
- Other (e.g. cancellation fees for accommodation and unsuccessful implementation of software) – R513 million (50%) (2015-16: R347 million [32%])

Of the R1 023 million incurred in 2016-17, only R16 million (2%) was incurred by auditees to **avoid further fruitless and wasteful expenditure** or losses that often related to the cost of cancelling irregular contracts or the contracts of non-performers.

The following auditees were the **main contributors** (72%) to fruitless and wasteful expenditure in 2016-17. The corresponding figures for 2015-16 are shown in *italics*.

Table 1: Highest contributors to fruitless and wasteful expenditure

Auditee	Amount (million)	Nature
Sapo	R194 *(2015-16: R7)*	The expenditure was the result of the payment of interest and penalties on overdue accounts and late payments. Included in this amount was R26,976 million that related to fines, penalties and legal fees due to creditors not being paid as a result of Sapo's financial constraints during the previous financial year.
Cooperative Governance, Human Settlements and Traditional Affairs (LP)	R109 *(2015-16: R2)*	The expenditure was caused by overpayments of R109 million for the acquisition of land.
Education (EC)	R88 *(2015-16: R74)*	The expenditure was due to the use of incorrect learner numbers in allocating transfers to school. The payments in excess of the true numbers of learners were considered to be fruitless and wasteful expenditure.
Health (NW)	R77 *(2015-16: R15)*	A total of 92% of this expenditure related the following: • Supply and maintenance of equipment at Moses Kotane Hospital • Equipment, software, warranty and maintenance at Vryburg Hospital
SABC	R75 *(2015-16: R35)*	A total of 96% of this expenditure related to litigation and claims.
National Treasury	R70 *(2015-16: R0)*	An amount of R67 million was for technical support for the Oracle system not yet implemented and R2,5 million related to the leasing of office space for the Brics bank.
Coega Development Corporation	R41 *(2015-16: R14)*	The expenditure was the result of the payment of interest and penalties on overdue accounts and late payments. Penalties and interest included income tax penalties and interest charged on the incorrect application of income tax requirements.
Human Settlements (GP)	R31 *(2015-16: R15)*	The expenditure was caused by the payment of interest and penalties on overdue accounts and late payments. Penalties and interest included payments for houses that needed to be repaired because they had been vandalised.
Acsa	R31 *(2015-16: R19)*	This amount related to a fine by the South African Revenue Service.

Auditee	Amount (million)	Nature
Financial and Accounting Services Sector Education and Training Authority	R22 *(2015-16: R0)*	This was as a result of a duplicate payment made in 2005-06 to a training service provider for services that had already been paid. This was identified as a result of an investigation commissioned by the accounting authority into irregular expenditure to the said service provider. The entity initially made a payment to the service provider for the training services provided. Subsequently, the entity received grants from a stakeholder that were also paid to the same service provider for the same training services already paid for.

These auditees are among those that had incurred fruitless and wasteful expenditure for the past three years, except for the National Treasury, Coega Development Corporation and Financial and Accounting Services Sector Education and Training Authority. Cooperative Governance, Human Settlements and Traditional Affairs in Limpopo, Education in Limpopo, Health in North West and the SABC had also incurred this type of expenditure for the past four years.

As detailed earlier on in this section, **inadequate action taken** by accounting officers and authorities to prevent fruitless and wasteful expenditure was one of the most common material findings on compliance. We reported the findings on compliance as material at 56 auditees (14%) (2015-16: 69 [19%]) based on the fact that they incurred fruitless and wasteful expenditure in the year under review as well as in previous years, a recurrence of the action that had caused the expenditure, and our assessment that adequate controls and processes would have prevented it.

Figure 1 further illustrates that we had identified only 18% of the fruitless and wasteful expenditure amount during the audit process, which means that most auditees had adequate processes to detect and quantify all such expenditure as required by legislation. This was a slight improvement from the previous year.

A

Annexure 1 available on our website shows the auditees that had incurred fruitless and wasteful expenditure.

9.3 Fraud and consequence management

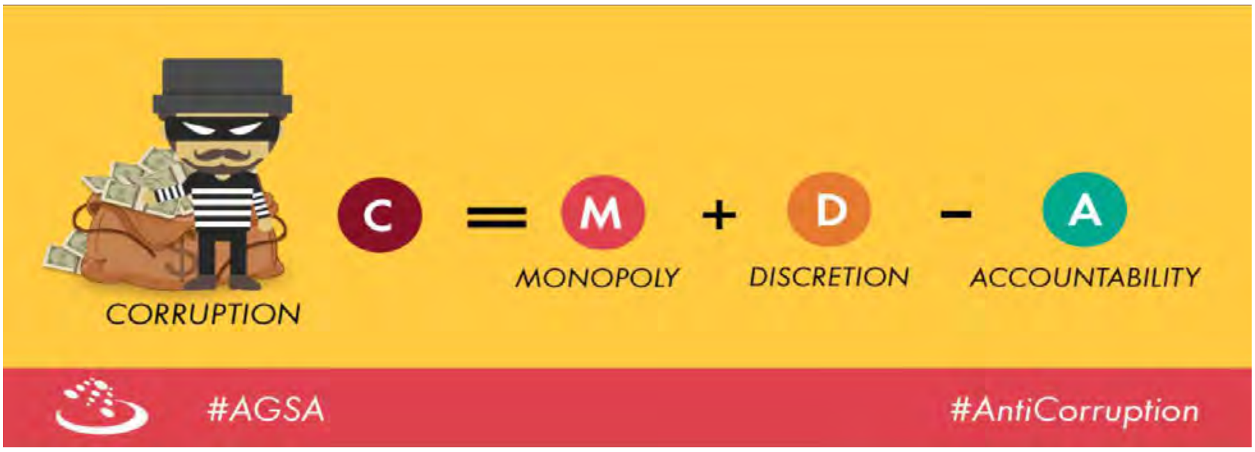
9.3 Fraud and consequence management

Accountability for government spending can be improved through acting in a consistent and deliberate manner against those officials who intentionally fail to comply with legislation or who are guilty of fraud or misconduct.

The PFMA and its regulations clearly stipulate that management should investigate matters such as incurring unauthorised, irregular and fruitless and wasteful expenditure, the possible abuse of the SCM system (including fraud and improper conduct), and allegations of financial misconduct and possible fraud. Appropriate actions should be taken based on the outcomes of these investigations.

Auditees with **poor consequence management** practices are often prone to corruption or fraud, as a result of officials not being held accountable. Figure 1 below demonstrates the need for strong accountability based on a formula on corruption developed by Robert Klitgaard.

Figure 1: Corruption formula



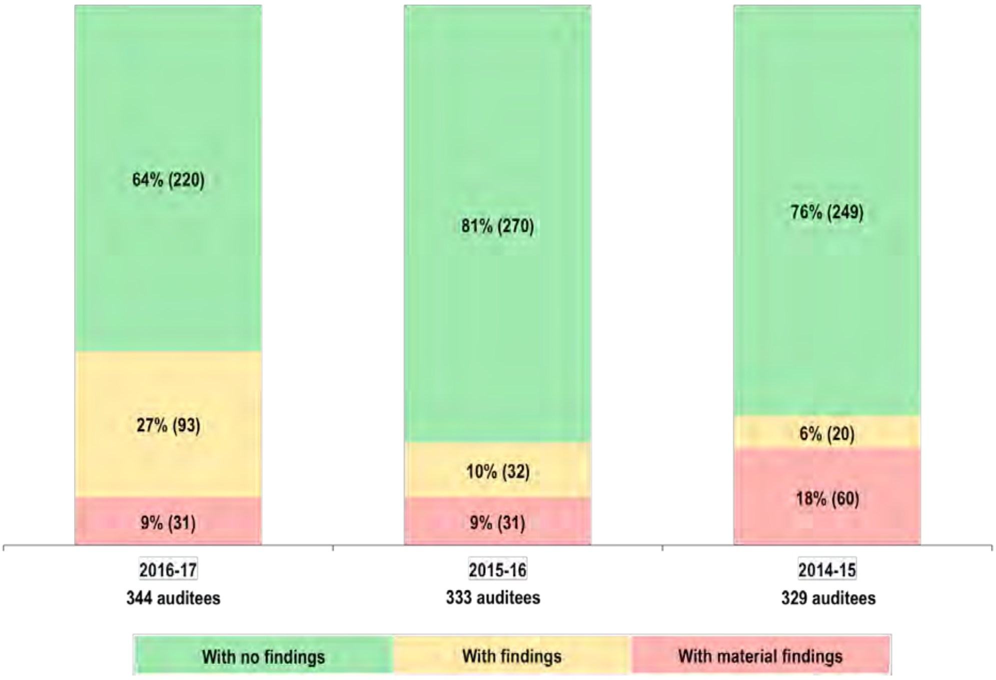
Corruption arises when officials are given sole power (**monopoly**) to make consequential decisions (**discretion**) without adequate oversight or control (**accountability**). In both national and provincial government, auditees are tasked with the responsibility of providing a number of services that cannot be provided by any other service provider, such as water and sanitation. When making financial decisions, auditees have a certain degree of discretion. In some cases, they decided to deviate from procurement processes as a result of, for example, bad planning. Should the accountability culture not be strong, these actions can create an environment that is conducive to corruption.

This section provides our observations and findings on how auditees managed allegations of misconduct and fraud, and how they dealt with unauthorised, irregular as well as fruitless and wasteful expenditure.

Non-compliance with legislation on consequence management

Figure 2 shows the extent of non-compliance with legislation in respect of consequence management since 2014-15 when we started auditing this area of compliance – ‘material findings’ means that the non-compliance was so significant that we reported it in the audit reports of those auditees, while ‘with findings’ means that there was non-compliance but to a lesser degree.

Figure 2: Status of consequence management



The **level of compliance with legislation on consequence management had regressed** since 2014-15 and significantly since the previous year. Although material non-compliance remained at the improved status of 9% we had reported last year, the increase in the number of non-material findings is concerning.

A total of 49 auditees that had consequence management findings in the previous year also had findings in the current year, while only 14 auditees had addressed the 2015-16 findings. A total of 75 auditees had consequence management findings for the first time in 2016-17 – this could be as a result of the continued improvements in our audit approach that allow us to identify allegations of financial and SCM misconduct and fraud and to report on how the auditee is dealing with these allegations.

The highest number of auditees with compliance findings in 2016-17 was in national departments and public entities (41), North West (20) and KwaZulu-Natal (13). The most common findings were the following:

- Irregular expenditure identified in the prior year was not investigated at 56 auditees.
- Fruitless and wasteful expenditure identified in the prior year was not investigated at 55 auditees.

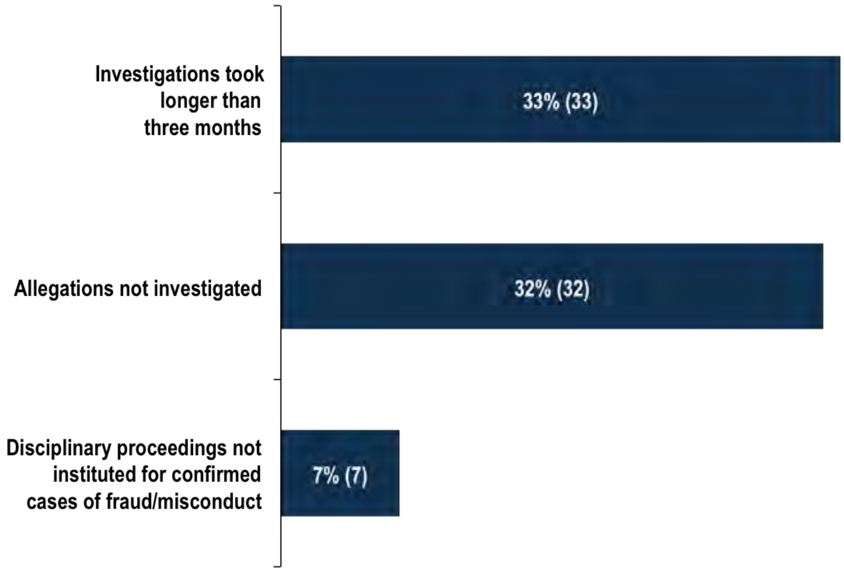
The remainder of this section provides more insights into the non-compliance and overall consequence management practices.

Reporting and follow-up of allegations of financial and supply chain management misconduct and fraud

Our audits showed that only 43 auditees (13%) **did not have all of the required mechanisms for reporting and investigating transgressions or possible fraud**, which included a lack of policies for investigation (20 auditees) and poor record keeping (26 auditees). Although 87% had the required mechanisms, these had not necessarily been successfully implemented.

Of the 99 auditees where allegations of misconduct or fraud were required to be followed up in 2016-17, 67 (68%) **did not take the appropriate action**. Figure 3 reflects our findings on how these allegations were dealt with.

Figure 3: Follow-up of allegations of financial and supply chain management misconduct and fraud



These findings were mostly in North West (19 auditees), the national sphere (18 auditees) and the Eastern Cape (11 auditees).

We recommend the following in this regard:

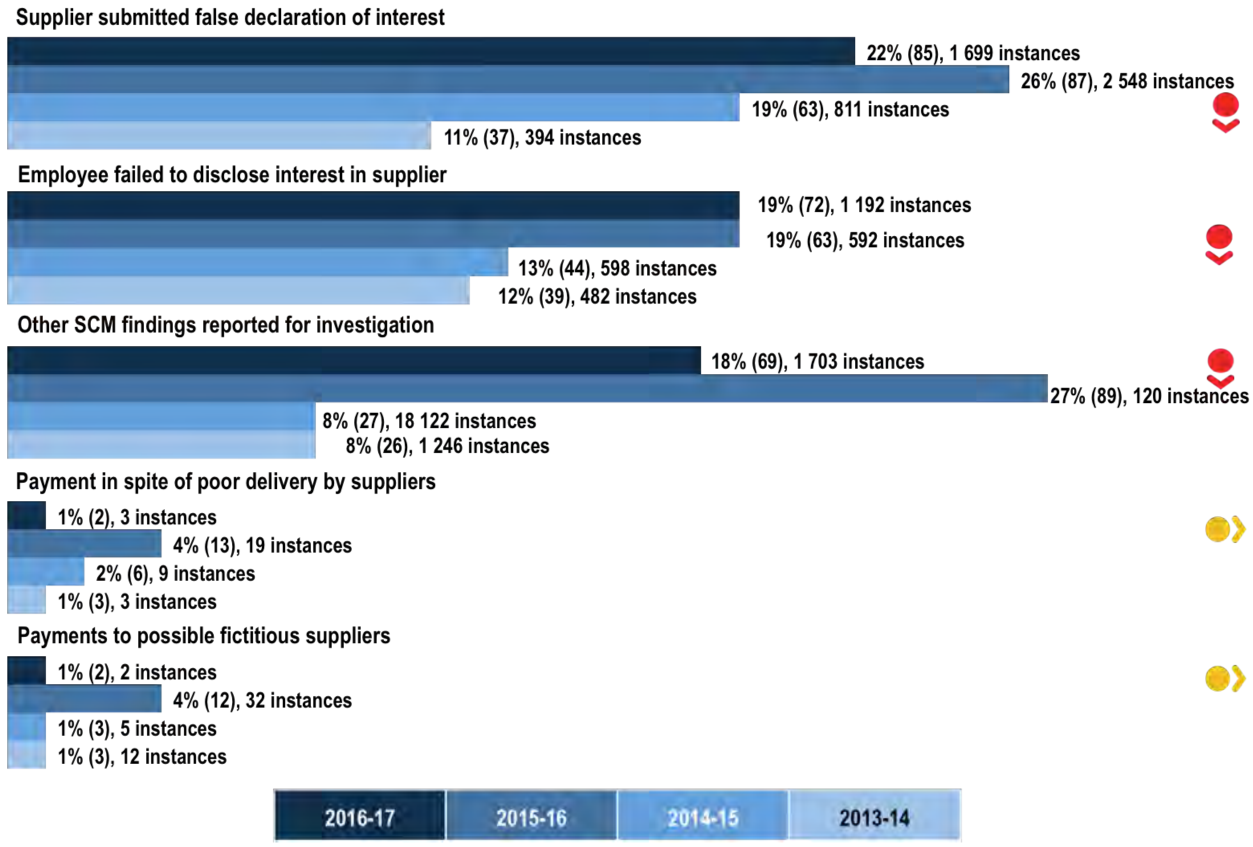
- Adopt systems (policies) to investigate allegations of misconduct and disciplinary procedures.
- Formally assign roles to investigate allegations to officials, units or committees of auditees.
- Properly investigate all allegations and take appropriate action based on the results of the investigation.
- Swiftly deal with investigations – the best practice in this regard is three months.
- Boards, audit committees and accounting officers should monitor and oversee the completion of the investigations to ensure that the process is comprehensive and fair, and leads to consequences where applicable.

Supply chain management findings reported for investigation

We report all our findings on SCM compliance and weaknesses to management for follow-up. If there are **indicators of possible fraud or improper conduct in the SCM processes**, we recommend that management conduct an investigation. The findings recommended for investigation are highlighted in the executive summary of our management reports to ensure that the accounting officer or authority, executive authority and audit committee take note thereof.

Figure 4 illustrates the extent of SCM findings we had reported to management for investigation in the past four years.

Figure 4: Supply chain management findings reported to management for investigation



In 2016-17, we reported these types of findings at 147 auditees (39%), which was an improvement from the 151 (46%) in 2015-16 but a regression from the 66 (20%) in 2013-14. In total, 106 (70%) of the 151 auditees that had such findings in 2015-16 had similar findings in 2016-17. Of the 147 auditees where we reported SCM findings for investigation, 102 were departments and 45 were public entities.

There had been an increase in all types of findings reported over the four-year period, except with regard to payments to possible fictitious suppliers and poor delivery by suppliers, which both remained the same. The number of auditees where we reported findings had decreased since the previous year except for the lack of disclosure by employees, which was reported at more auditees with the number of instances more than doubling. Section 9.1 includes more information on our findings in this regard.

The lack of improvement was as a result of accounting officers or authorities not investigating our findings and ensuring that there were consequences for non-compliance and transgressions.

Figure 5 shows whether all, some or none of the previous year's SCM findings reported for investigation had been investigated.

Figure 5: Follow-up of the previous year's supply chain management findings

Although 68 of the 151 auditees (45%) investigated all of the SCM findings reported for investigation in the previous year, the fact that just over a third of these auditees (51) had investigated none of the findings is concerning. Of these 51 auditees, 36 were departments and 15 were public entities. Auditees were also clearly reluctant to deal with the conflict of interest matters, as only 32% of them had been investigated.

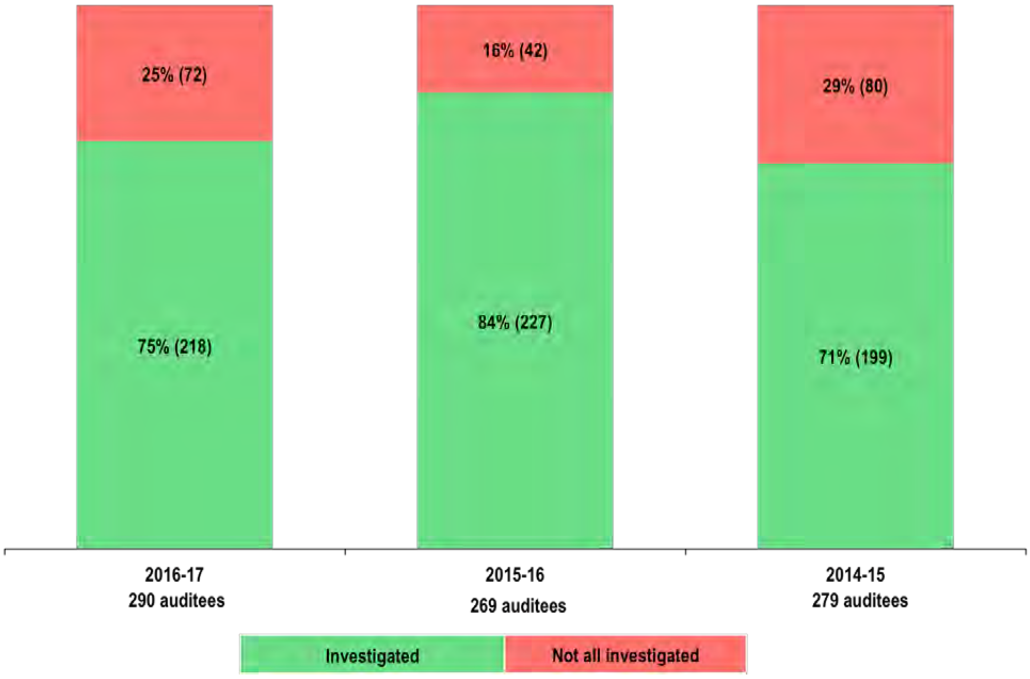
The highest number of auditees where none of the SCM findings reported for investigation in the previous year had been investigated was in the national government (13) (which included the Department of Home Affairs, the Department of Public Works and Sapo), North West (12) and Mpumalanga (seven).

We recommend that auditee management pay urgent attention to the findings we report for investigation, as these could be indicators of fraud and/or could lead to financial loss.

Investigation and follow-up of unauthorised, irregular and fruitless and wasteful expenditure

Figure 6 shows the overall status of investigations at the auditees that had incurred unauthorised, irregular and fruitless and wasteful expenditure in the previous year over a three-year period.

Figure 6: Investigation of unauthorised, irregular and fruitless and wasteful expenditure

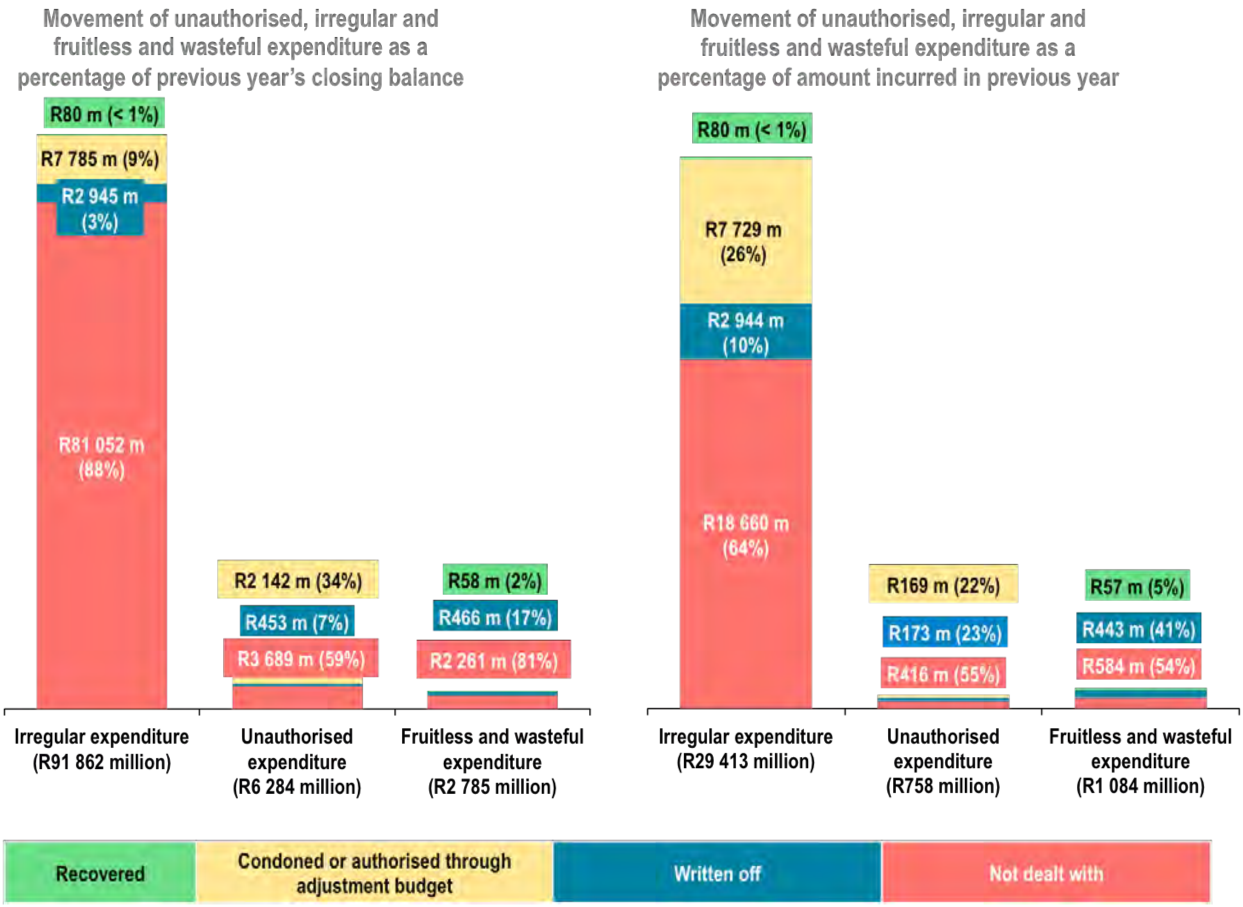


At just 75% of the auditees, the accounting officer or authority **conducted the required investigations into all instances** of unauthorised, irregular and fruitless and wasteful expenditure. This was a regression from the 84% in the previous year but a slight improvement since 2014-15. A total of 29 of the 42 auditees (69%) that did not conduct investigations in 2015-16 again did not do so in 2016-17.

Although investigations were conducted at most of the auditees, **sufficient steps were not taken to recover, write off, approve or condone** unauthorised, irregular and fruitless and wasteful expenditure as required by legislation. As a result, the year-end balance of irregular expenditure that had accumulated over many years and had not been dealt with totalled R126,08 billion, while that of unauthorised expenditure was R5 156 million and that of fruitless and wasteful expenditure was R3 283 million.

Figure 7 shows that only a small portion of unauthorised, irregular and fruitless and wasteful expenditure of the previous years and the current year had been properly dealt with in the current year.

Figure 7: Movement in unauthorised, irregular and fruitless and wasteful expenditure balances



It is encouraging that the unauthorised expenditure that had accumulated over many years had decreased by R1 128 million (18%) to R5 156 million since the previous year. However, over 50% of the unauthorised, irregular and fruitless and wasteful expenditure incurred in the previous year had not been properly dealt with. This is a sure sign that consequences and follow-through relating to unauthorised, irregular and fruitless and wasteful expenditure are seriously lacking. Although these types of expenditure are investigated at most auditees, limited or no action is taken after the investigation.

The fact that auditees cannot condone their own irregular expenditure also played a role in the accumulation of this expenditure. Auditees have to request condonement from the 'owners' of the legislation that had been transgressed, mostly the National Treasury. This typically requires additional information and takes some time to be considered.

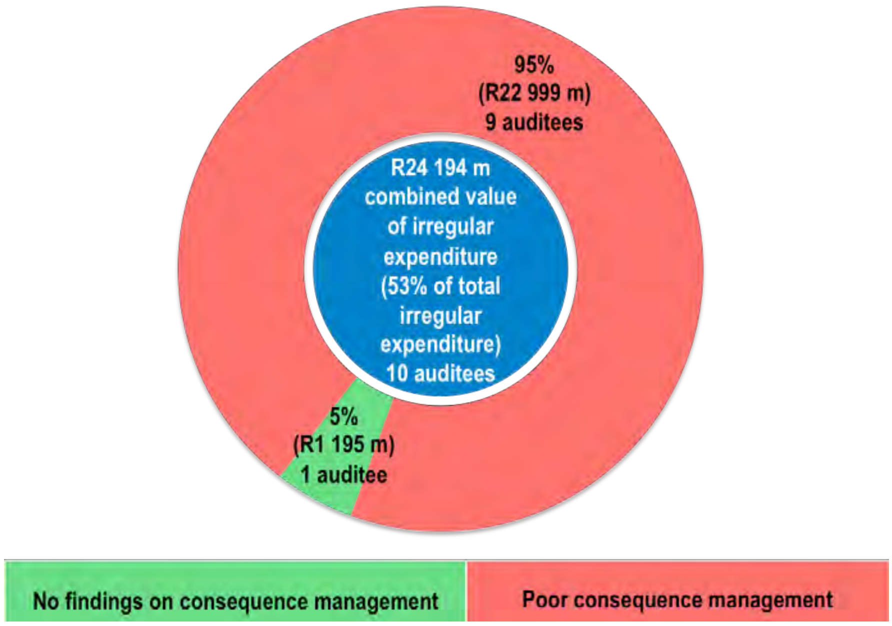
Unauthorised, irregular and fruitless and wasteful expenditure incurred should be dealt with by the accounting officer or authority. We therefore recommend that the accounting officer or authority:

- properly investigate all instances of unauthorised, irregular and fruitless and wasteful expenditure to determine if any official is liable for the expenditure
- recover the resultant loss if the investigation determined that an official was liable, unless the expenditure is irrecoverable and disciplinary processes follow
- in cases of irregular expenditure, request condonation from the National Treasury of contraventions of the PFMA or its regulations – only if the non-compliance had no impact or negligence was not proven
- report all cases of irregular expenditure that constitutes a criminal offence to the police
- in cases of unauthorised expenditure, authorise it through an adjustment budget.

Highest contributors to irregular expenditure linked to poor consequence management

Figure 8 highlights the correlation between poor consequence management practices and the highest contributors to irregular expenditure, as detailed in section 9.1.

Figure 8: Correlation between poor consequence management practices and the highest contributors to irregular expenditure



All of the 10 highest contributors, except Roads Agency Limpopo SOC Ltd, had poor consequence management practices, five of which had such poor consequence management practices relating to irregular expenditure.

Conclusion

As long as the political leadership, senior management and officials do not make accountability for transgressions a priority, irregular, unauthorised and fruitless and wasteful expenditure as well as fraud and misconduct will continue. An environment that is **weak on consequence management is prone to corruption and fraud** and the country cannot allow money intended to serve the people to be lost. Most auditees have the required policies and processes to ensure that transgressions and fraud are identified and acted upon, but chose not to use it – a clear indicator of a lack of commitment to accountability.

NOTES

10 Status of internal control

10. Status of internal control

What are internal controls?

Internal controls are processes and measures instituted by an auditee to:

- ensure that it meets its mandated objectives
- conduct its business in an effective, efficient and economical manner
- safeguard its assets and resources
- deter and detect errors, fraud and theft
- ensure the accuracy and completeness of its accounting and performance information
- produce reliable and timely financial and non-financial reports
- ensure compliance with legislation and adherence to its policies and plans
- promote accountability and transparency.

Good **internal control** is the key to ensuring that auditees deliver on their priorities in an effective, efficient and economical manner. It will also ensure that auditees produce quality financial statements and performance reports, and comply with applicable legislation – especially in the area of procurement and contract management. It is the responsibility of accounting officers, chief executive officers, senior managers and officials to implement and maintain effective and efficient systems of internal control.

Figure 1 and table 1 show the status of the different drivers of internal control and their overall movement over the past four years. We determined the movements taking into account either increases in good controls or reductions in controls requiring intervention.

Figure 1: Drivers of internal control

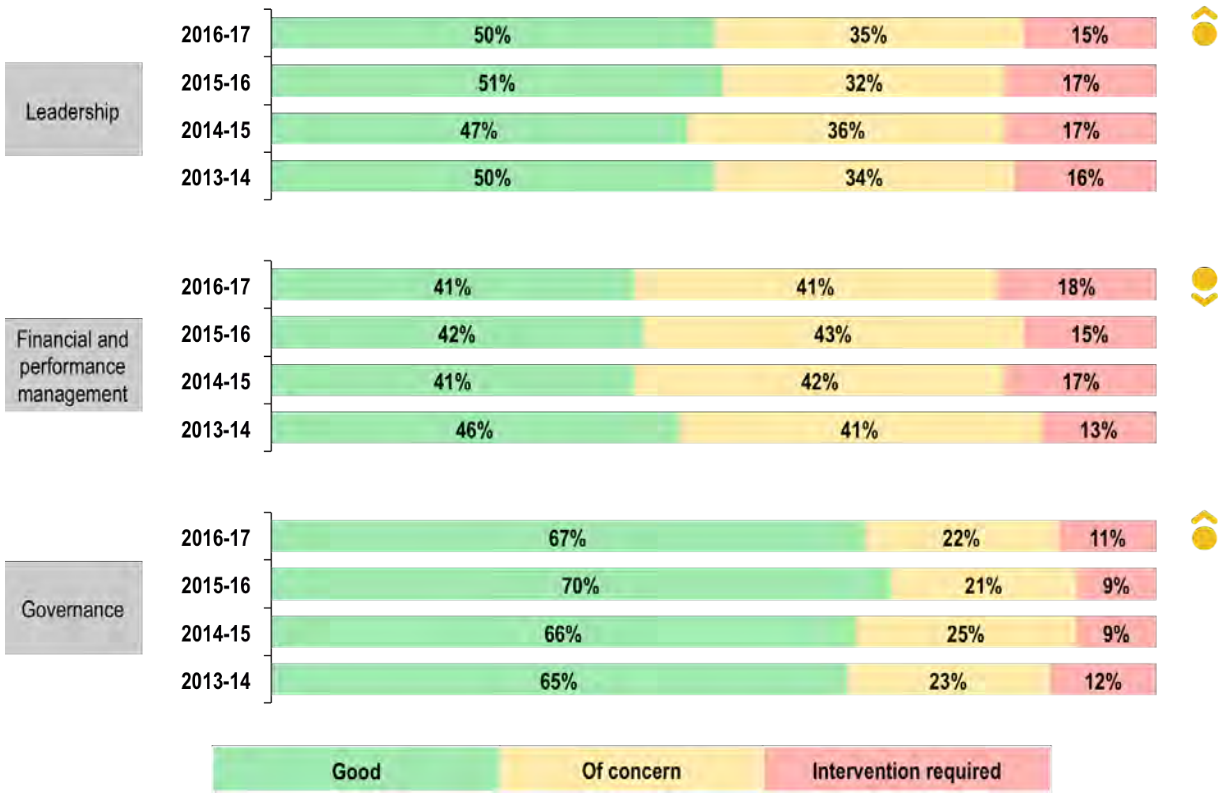


Table 1: Progress made in improving drivers of internal control in national and provincial government over four years

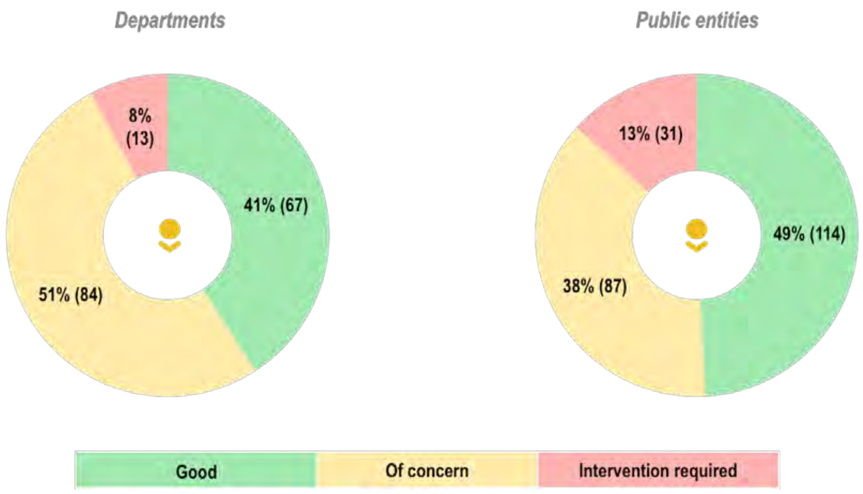
Portfolio	Leadership	Financial and performance management	Governance
National auditees			
Eastern Cape			
Free State			
Gauteng			
KwaZulu-Natal			
Limpopo			
Mpumalanga			
Northern Cape			
North West			
Western Cape			
Total			

As illustrated in figure 1, two of the three drivers of internal control had shown a slight improvement since 2013-14, with financial and performance management showing a slight regression over the four-year period. Leadership was the only driver of internal control that had improved slightly since the previous year, while financial and performance management as well as governance slightly regressed. This corresponds to the limited improvement in audit outcomes as detailed in section 6.1.

The lack of overall improvement was the result of the progress made by some national and provincial auditees being offset by the regression and stagnation of other auditees, as seen in table 1.

Figure 2 shows the overall status of internal control for departments and public entities.

Figure 2: Status of internal control of departments and public entities



Since the previous year, the overall status of departments and public entities that we have assessed as good had regressed slightly from 44% to 41% and from 50% to 49%, respectively. All the public entities in North West were assessed as requiring intervention, while the Free State had the highest number of departments in this category during 2016-17. A contributing factor to the regression at public entities was that 21% of the public entities did not have a **chief executive officer** at year-end – an indication of instability in the management of these entities and a lack of attention to their control environment.

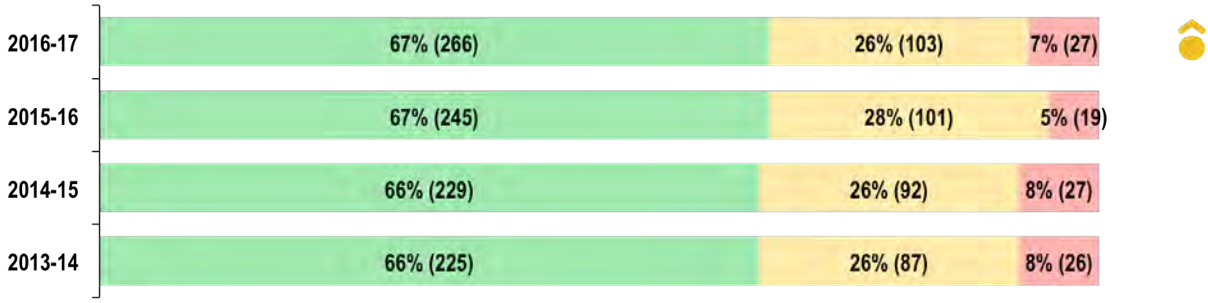
Basic controls

We discuss five of the seven basic controls that should receive specific attention in the remainder of this section, and discuss HR management and IT controls in sections 11 and 12, respectively. Figures 3 to 7 show the movement in these five basic control areas over the past four years.

The following legend applies to the figures shown:

Good	Of concern	Intervention required

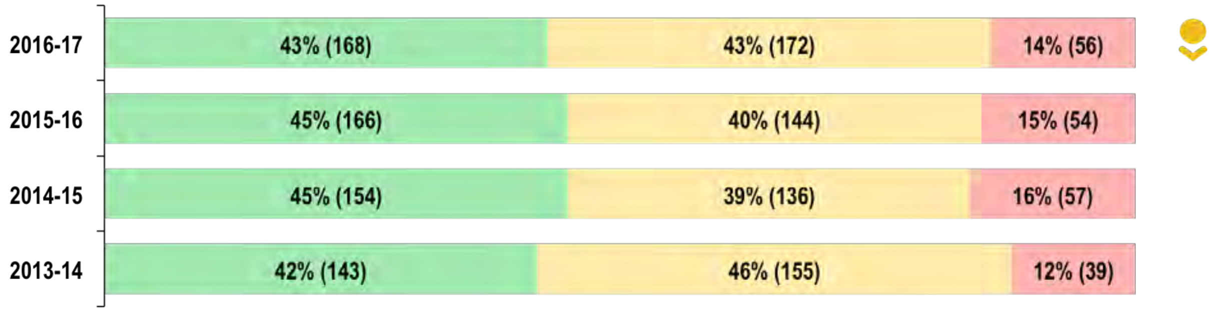
Figure 3: Effective leadership



In order to improve and sustain audit outcomes, auditees require **effective political and administrative leadership** that is based on a culture of honesty, ethical business practices and good governance, which protects and enhances the interests of the auditee.

Effective leadership controls had slightly improved over the four-year period, but slightly regressed from the previous year. Effective leadership controls were more prominent at public entities (72% – a slight regression from the previous year's 70%) than at departments (63% – a slight improvement from the previous year's 62%).

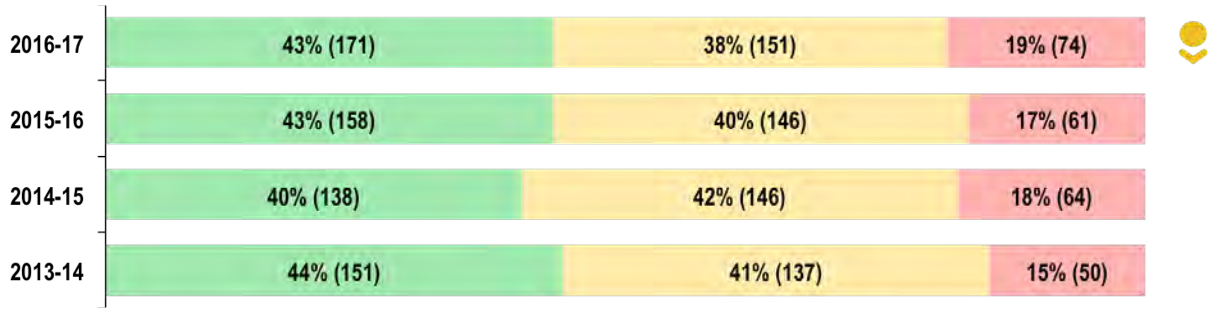
Figure 4: Audit action plans



Developing action plans and monitoring their implementation to address identified internal control deficiencies are key elements of internal control that are the responsibility of heads of departments, chief executive officers and their senior management teams.

The controls relating to audit action plans had regressed slightly over the four-year period and since the previous year. The reason for this was that in many cases audit action plans responded only to our audit findings and did not always address the associated root causes, while not all audit action plans that had been drawn up were fully implemented.

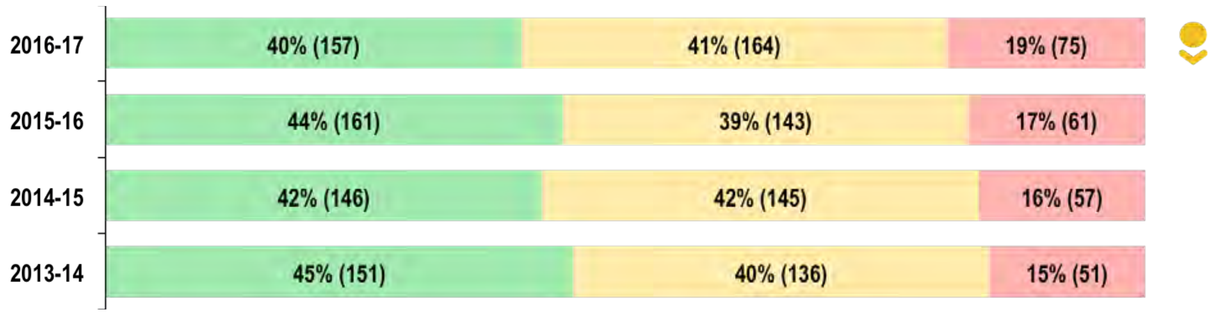
Figure 5: Proper record keeping



Proper and timely record keeping ensures that **complete, relevant and accurate information** is accessible and available to support financial and performance reporting. Sound record keeping will also enable senior management to hold staff accountable for their actions. A lack of documentation affects all areas of the audit outcomes.

Record-keeping controls had slightly regressed over the four-year period as well as since the previous year.

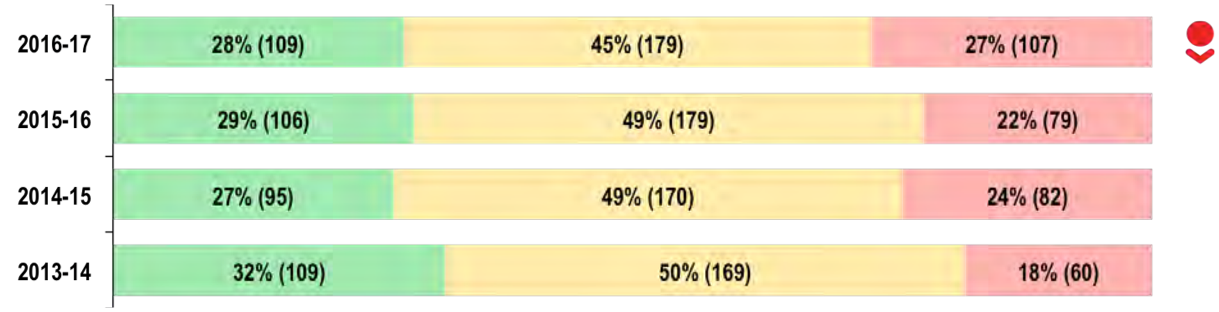
Figure 6: Daily and monthly controls



Controls should be in place to ensure that **transactions are processed in an accurate, complete and timely manner**, which in turn will reduce errors and omissions in financial and performance reports.

There had been a slight regression in the daily and monthly controls from 2013-14 as well as since the previous year. Good controls had been established at 34% of the departments and 44% of the public entities.

Figure 7: Review and monitor compliance



Auditees should have mechanisms that identify applicable legislation as well as changes to legislation, assess the requirements of legislation, and implement processes to ensure and monitor compliance with legislation.

The controls relating to **monitoring compliance** had regressed over the four-year period but only slightly so from the previous year. These controls continued to be the poorest control area at auditees. Many auditees did not comply with legislation, as detailed in section 9. This indicates that the internal controls of most auditees not only failed to prevent non-compliance with legislation, but also failed to timeously detect the deviations – some of which were only detected during, and responded to following, our audits.
In 2016-17, good controls had been established at 27% of the departments and 28% of the public entities.

Conclusion

Strong internal controls are the key to unlocking improvements in national and provincial government. If underlying weak internal controls are not addressed, it increases the risk of the misappropriation of funds, unreliable financial and performance reporting as well as non-compliance with legislation. On the other hand, a sound internal control environment that is monitored in a robust manner by the different assurance providers (as further discussed in section 13) will enable **effective, efficient and economical service delivery**, **accurate and reliable financial and performance reporting** as well as **compliance with legislation**. This in turn will facilitate accountability and transparency in the management of public funds.

11 Human resource management

11. Human resource management

Figure 1 provides the status of HR management controls over the past four years. Figure 2 shows the status of these controls for departments and public entities, while table 1 lists the number of auditees with good HR controls in national and provincial government.

Figure 1: Status of human resource management controls

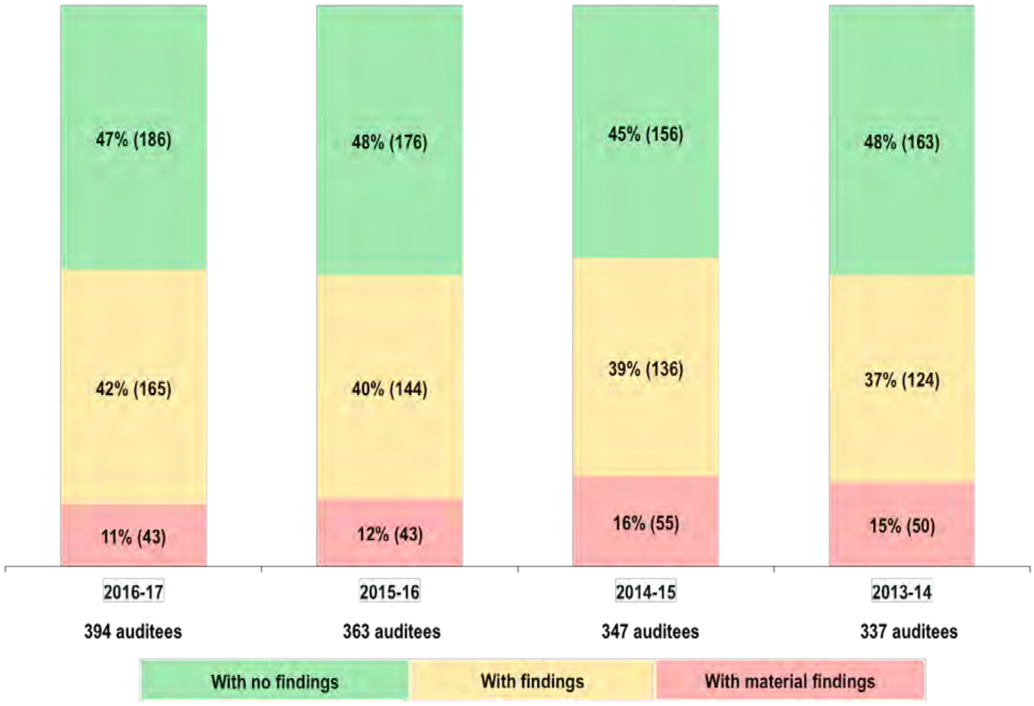


Figure 2: Status of human resource management controls – departments and public entities

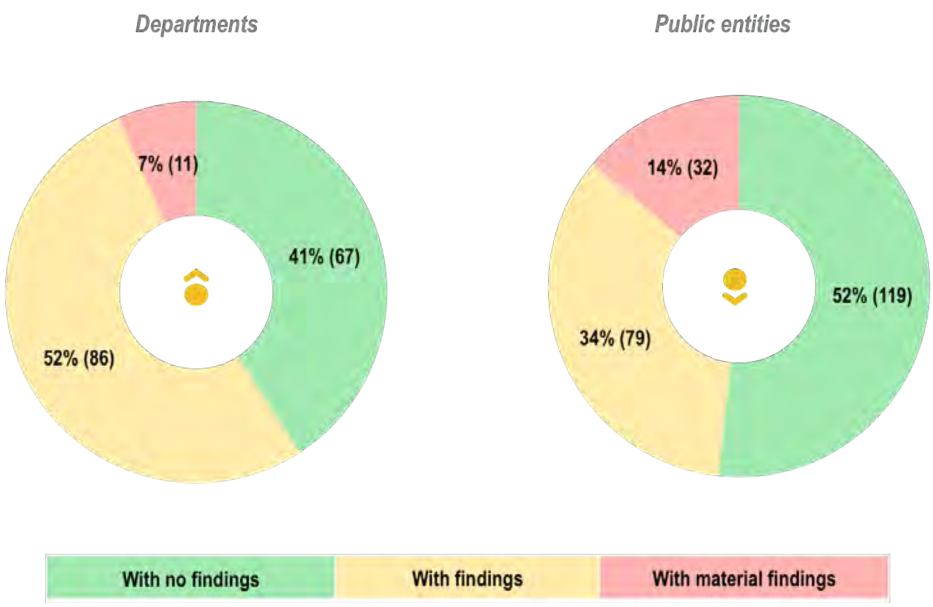


Table 1: Status of human resource management controls in national and provincial government

Portfolio	Auditees with good human resource management controls	Movement from 2015-16
National auditees	115 (53%)	
Eastern Cape	11 (52%)	
Free State	3 (19%)	
Gauteng	14 (61%)	
KwaZulu-Natal	10 (43%)	
Limpopo	5 (24%)	
Mpumalanga	4 (24%)	
Northern Cape	3 (23%)	
North West	2 (9%)	
Western Cape	19 (100%)	
Total	186 (47%)	

At an overall level, the number of auditees with good HR management controls had increased over the four years and from the previous year. As a result of the significant increase in the number of auditees at which we performed the assessment, percentages show a slight regression. The number of auditees requiring intervention remained the same as in the previous year, but was slightly lower than in 2013-14.

The HR controls at departments had slightly improved since the previous year, with only a slight regression at public entities. We assessed the HR management controls of one national department and 10 provincial departments as requiring intervention. Provincial public entities (45%) lagged behind national public entities (54%) in implementing and maintaining good HR controls.

Auditees in Gauteng, Limpopo and Mpumalanga showed improvement from the previous year, while the Free State and the Northern Cape regressed. It is commendable that all the auditees whose audits had been completed in the Western Cape maintained good HR controls.

Vacancies and stability

One of the biggest challenges for national and provincial government is to attract and retain qualified and competent persons in all areas of administration. As discussed in the NDP, there is an unevenness in capacity that leads to uneven performance in the public service.

The MTSF includes various actions to address the lack of capacity and sets targets to be achieved. One of these targets is to have a vacancy rate of less than 10% in national and provincial departments by 2019. This target has not been achieved yet, but the decrease in the vacancy rate at national and provincial departments from 17% to 12% over the past four years is encouraging.

The overall vacancy rate had slightly improved from 14% to 12% since the previous year as well as from 15% since 2013-14. The vacancy rate at senior management level was 15% in 2016-17 – a slight improvement from the 17% in the previous year. The senior management vacancy rate was also 15% in 2013-14.

As part of our audits, we considered the vacancies and resourcing of finance units, as inadequate capacity in these units negatively affects the management, control and quality of financial reporting. The **average vacancy rate** in finance units at year-end was 11% – a slight improvement from the 14% in the previous year and the 12% in 2013-14. In our assessment (based on vacancies and the skills of finance staff), the capacity of the finance units of 108 auditees (27%) either was concerning or required intervention.

We also considered **vacancies in key positions** at year-end and **stability** in those positions. These key positions include heads of departments, chief executive officers, chief financial officers and heads of SCM units. Figures 3 to 6 provide a four-year overview of the number of auditees where these positions were vacant at year-end as well as the period that the positions had been vacant. They further show the average number of months the current incumbents had been in their positions.

Figure 3: Heads of departments – vacancy and stability

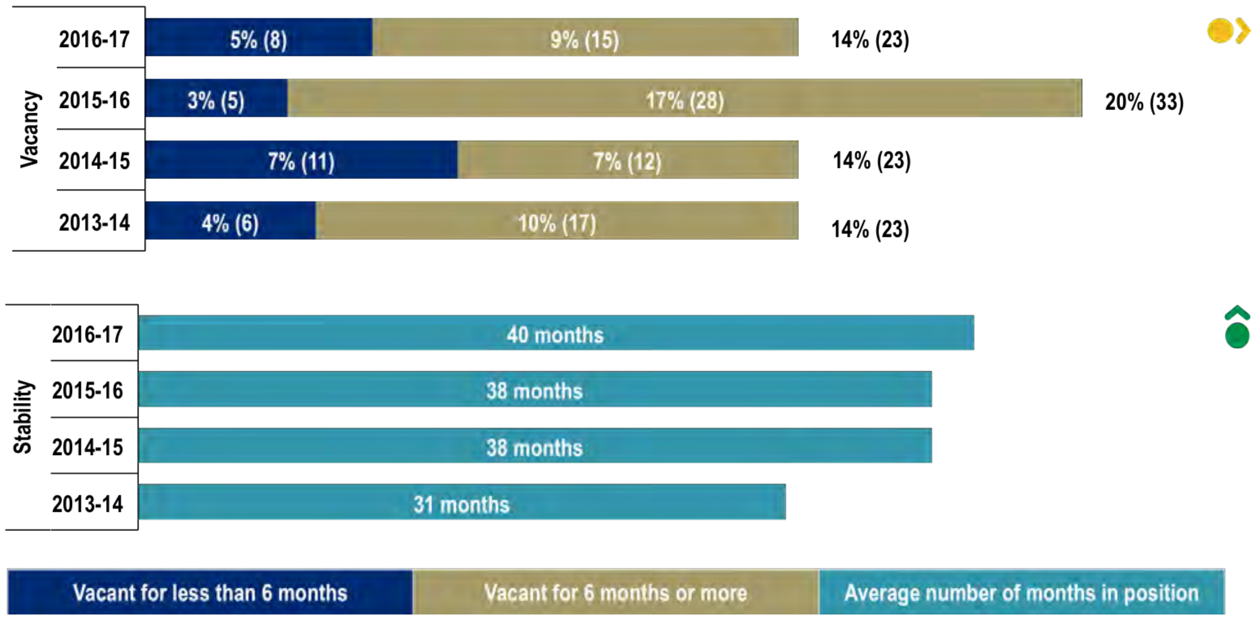
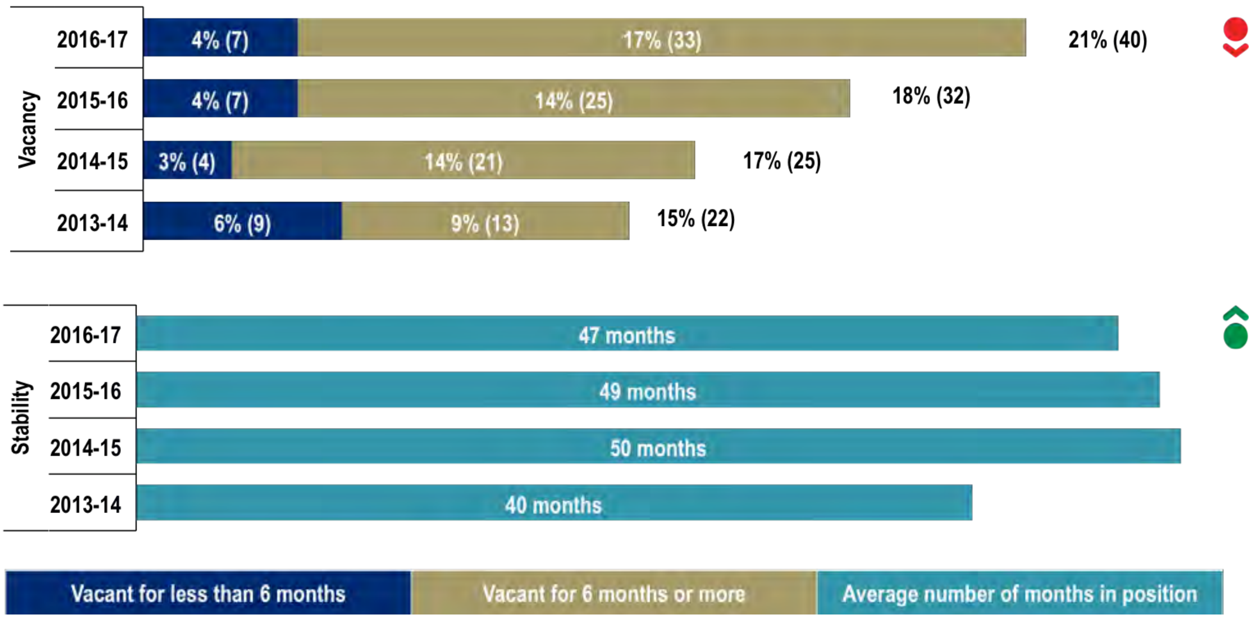


Figure 3 shows that the vacancy rate of **heads of departments** had improved from the previous year but remained at the same level as in 2013-14. The departments in Limpopo (from 46% to 15%), North West (from 31% to 8%), Mpumalanga (from 8% to 0%), the Western Cape (from 8% to 0%) and the Northern Cape (from 38% to 31%) were the main contributors to the improvement since the previous year. There had also been a slight improvement at national departments since the previous year.

The MTSF includes targets to retain heads of departments for at least four years by 2019. This target has not been achieved yet, but the improvement from 31 months to 40 months since 2013-14 is encouraging. There had been a slight improvement in the average length of time heads of departments had been in their position since the previous year. By 2016-17, heads of departments at 64 departments (45%) had been in the position for three years or longer – an improvement from the 52 (39%) in 2013-14 and a slight improvement from the 57 (44%) in the previous year.

Figure 4: Chief executive officers – vacancy and stability



As reflected in figure 4, over a fifth of the public entities did not have a **chief executive officer** at year-end. The vacancy rate at this level increased every year in the past four years, creating instability in the management of these entities. Most of these 40 public entities were in the national sphere (31), and included 13 public entities in the higher education and training portfolio (mostly TVET colleges and sector education and training authorities), the Financial and Fiscal Commission, the Municipal Infrastructure Agency, and the Strategic Fuel Fund.

The average length of time that chief executive officers had been in their position was almost four years in 2016-17 – an improvement when compared to 2013-14 when it stood at 40 months. By 2016-17, chief executive officers at 57 public entities (36%) had been in the position for four years or longer – a slight regression from the 58 (41%) in the previous year but a slight improvement when compared to the 38 (31%) in 2013-14.

Figure 5: Chief financial officers – vacancy and stability

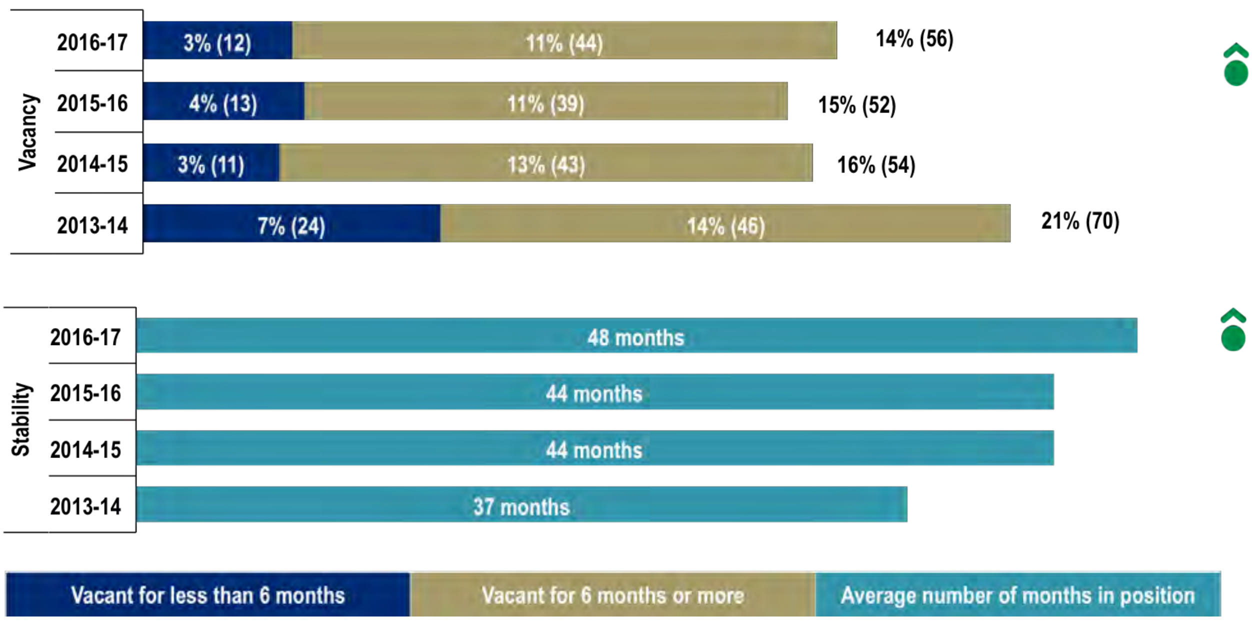


Figure 5 shows that the **chief financial officer** vacancy rate at auditees had improved since 2013-14, with a slight improvement from the previous year in the percentage (the number shows a regression, but it is as a result of a significant increase in the number of auditees being audited since 2015-16). Most of the auditees without chief financial officers in 2016-17 were in national government (29), KwaZulu-Natal (four) and Limpopo (four).

The average length of time that chief financial officers had been in their position had improved from the previous year, with a significant improvement from just over three years in 2013-14 to four years in the current year. By 2016-17, chief financial officers at 131 auditees (39%) had been in the position for four years or longer. This was a significant improvement compared to the 114 auditees (37%) in the previous year and the 84 auditees (32%) in 2013-14.

Figure 6: Heads of supply chain management units – vacancy and stability

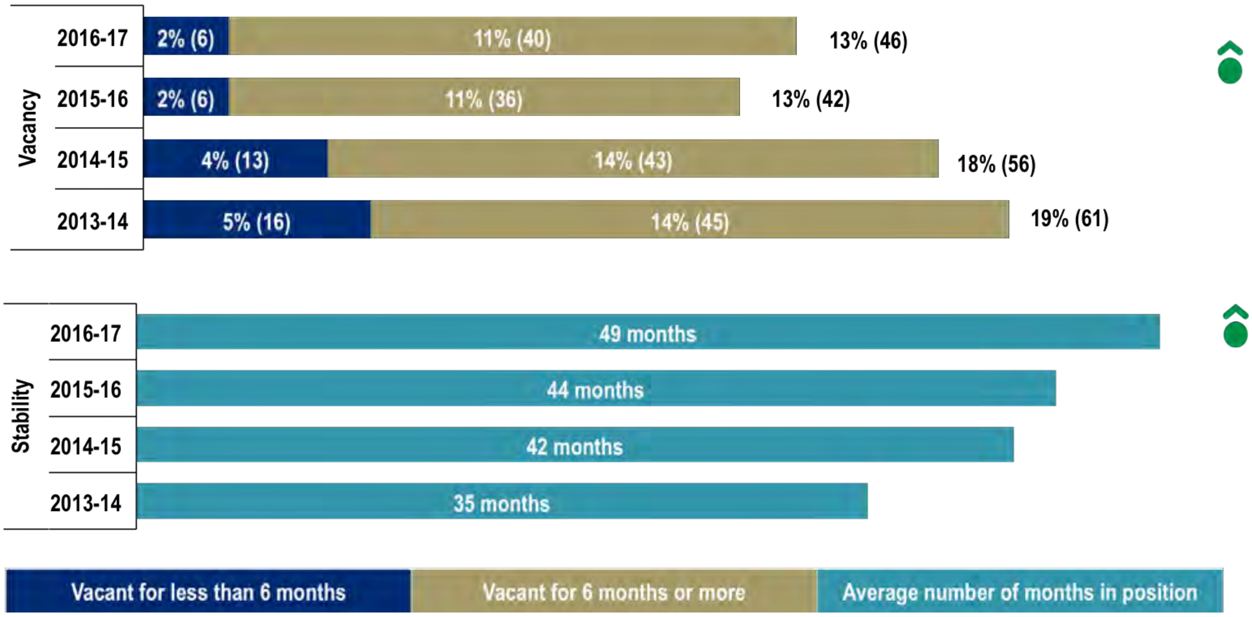


Figure 6 shows that the vacancy rate for **heads of SCM units** had improved since 2013-14, with a slight regression from the previous year. In 2016-17, only 39 auditees (mostly public entities) did not have a dedicated position for this role, with the work being performed mostly by the chief financial officer.

The average number of months that the heads of SCM units had been in their position had improved since the previous year as well as since 2013-14. By 2016-17, heads of SCM units at 121 auditees (39%) had been in the position for four years or longer – an improvement from the 89 (31%) in the previous year and the 75 (29%) in 2013-14.

Conclusion

Good HR management practices are a foundation for strong internal controls, as vacancies and inadequate skills affect the establishment, execution and monitoring of control activities. Our recommendations for improving HR management are included in section 15.

A

Annexure 1 available on our website lists all auditees and the status of their HR management controls.

12 Information technology controls

12. Information technology controls

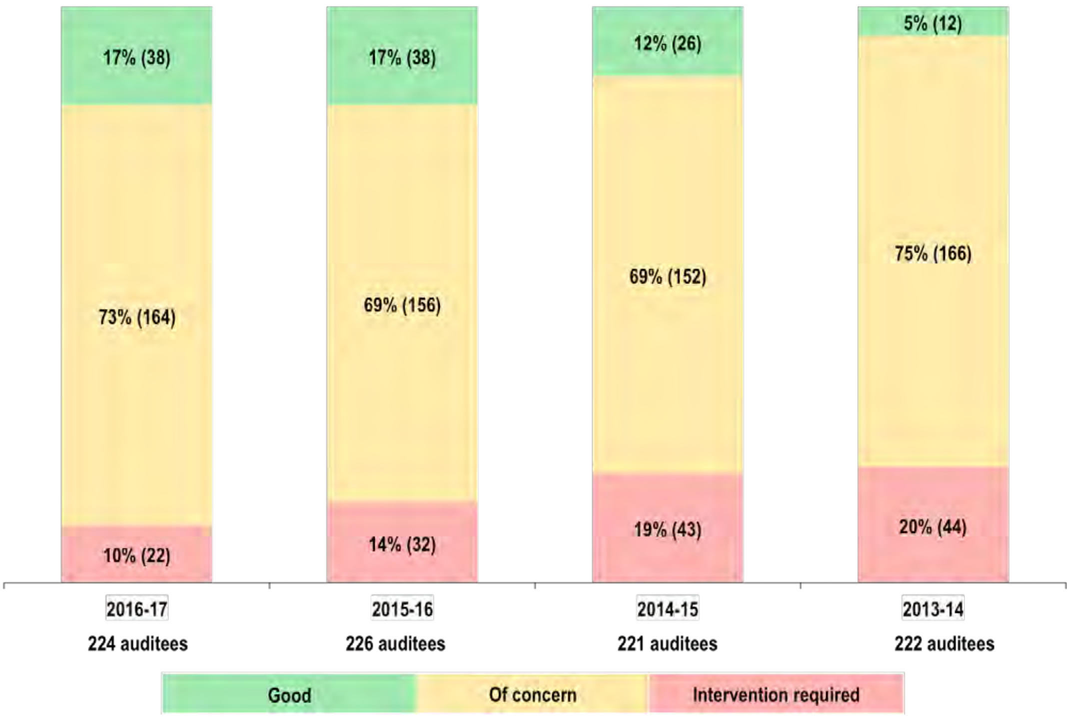
An inherent part of the control environment in national and provincial auditees is the status of their IT controls. **IT controls** ensure the **confidentiality, integrity** and **availability** of state information, enable **service delivery** and promote national **security**. It is thus essential for good IT governance, effective IT management and a secure IT infrastructure to be in place.

Effective IT governance underpins the overall well-being of an auditee's IT function and ensures that the auditee's IT control environment functions well and enables service delivery. As the majority of financial management controls are automated and monitoring takes place mostly on reports generated by the IT systems, good IT controls and skills are fundamental to enabling robust financial management systems (**DO**) and in-year monitoring (**CHECK**).

Overview of the status of information technology focus areas

Figure 1 shows the status of IT controls since 2013-14.

Figure 1: Status of information technology controls



We assessed IT controls at 224 national and provincial auditees with more complex IT environments and found that the number of auditees that had good IT controls increased significantly over the past four years from 5% in 2013-14 to 17% in 2016-17. The improvements were generally due to these auditees becoming more capacitated and taking accountability for their IT environment, but quicker responses are required. We had assessed 226 national and provincial auditees in 2015-16 as opposed to the 224 this year, due to two auditees not signing off on the audit reports as per the deadlines.

Our audits included an assessment of the IT controls in the areas of **security management, user access management** and **IT continuity**. Figure 2 outlines the status of controls in the areas we audited and indicates, per focus area, whether the IT controls were good, concerning or required intervention.

Figure 2: Status of information technology focus areas

There had been an improvement over the past three years in all focus areas and a slight stagnation in the last year, with a significant decrease in the number of national and provincial auditees where intervention was required, indicating that they were moving in the right direction.

Figure 3 further shows an improvement for both departments and public entities from the previous year. The percentage of auditees with a good IT control environment was more or less equal; however, significantly fewer public entities required intervention than departments, due to those charged with governance taking accountability for addressing IT control weaknesses and more staff within the IT sections that were qualified and skilled. However, we remain concerned about the number of public entities at which the IT controls were concerning or required intervention, as the majority of public entities were supported by complex IT environments that were very dependent on adequate IT controls and monitoring by the different assurance providers.

Figure 3: Status of information technology controls – departments and public entities

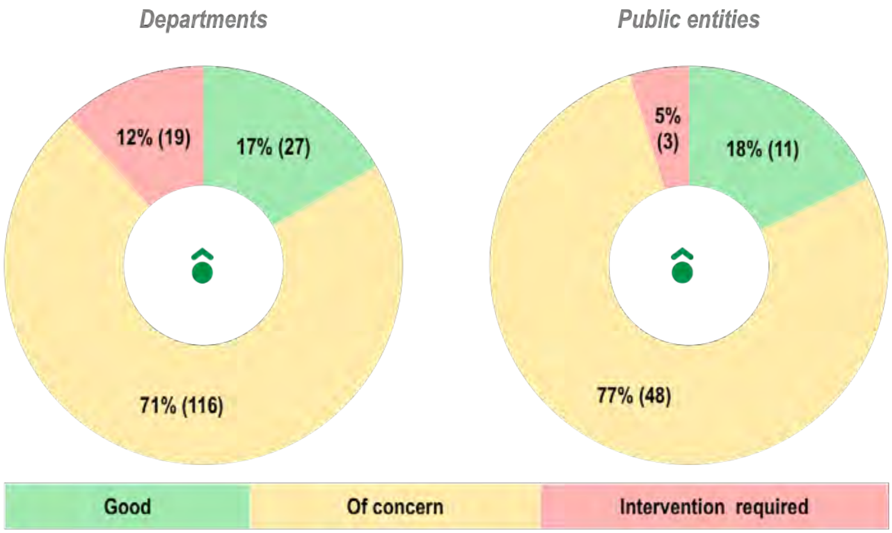


Table 1 indicates the **progress made** since the previous year in addressing areas of concern at national and provincial departments as well as at public entities.

The improvements were generally due to the following:

- More auditees employing chief information officers or IT managers with **adequate qualifications and experience**.
- Auditees **implementing some recommendations** made by the internal and external auditors.
- In Mpumalanga, the **government IT officers** played a **key role** additional to the above-mentioned; and in North West, improvements were mainly due to the **active role** that the **system controllers** played.

Table 1: Progress made in improving information technology controls

Portfolio	Security management	User access management	IT continuity
National departments	↓	↓	↑
Eastern Cape	↓	↑	↑
Free State	↓	↓	↑
Gauteng	↓	↑	↓
KwaZulu-Natal	↓	↓	↓
Limpopo	↑	↓	↑
Mpumalanga	↑	↑	↑
Northern Cape	↓	↓	↑
North West	↑	↑	↑
Western Cape	↑	→	↓
Public entities	↑	→	↓

The **most common findings** were the following:

- Although national and provincial auditees were moving in the right direction and there had been an improvement over the three years overall, the basic IT controls had still not been adequately defined and implemented at most auditees in all three focus areas. Policies and procedures had not been designed or implemented, as also reported in the previous year. Furthermore, the security controls of five provinces and the national departments regressed despite the fact that a number of auditees were still experiencing attacks through their network exposing them to various vulnerabilities, which may have been prevented if security controls had been adequate.
- It is concerning that KwaZulu-Natal regressed in all three areas. This was due to inadequate funding, a shortage of in-house IT skills on lower levels, and systems having functionality limitations.
- A further concern is the regression in two of the three focus areas in the Free State, the Northern Cape, Gauteng and the national departments. This was mainly due to vacancies and a shortage of IT skills on lower levels, budget constraints, and a lack of oversight to ensure that corrective actions were taken and monitored.
- User access weaknesses remained a challenge at the majority of auditees due to a lack of segregation of duties, inadequate reviews of system administrator activities and excessive user access rights. In the case of departments that use transversal systems, the data hosted on these systems is available at the disaster recovery site of the State Information Technology Agency (Sita). However, many departments still did not participate in the Sita transversal disaster recovery testing, as we have reported for the past four years. Where systems are not hosted by Sita, departments and entities have to provide their own data recovery strategies. However, the majority of these auditees still did not have adequate disaster recovery plans and did not test their backups to ensure that they could be restored when required. This could have a major impact on service delivery as the availability of systems is crucial to the achievement of outcomes.
- Public entities continued to increasingly implement enterprise resource planning systems. The enterprise resource planning and project review audits revealed that these systems were not appropriately configured and business requirements were not appropriately documented, resulting in implementations failing or being signed off without understanding the return on investment of these projects. As a result, many of these implementations did not support business objectives and efficiency improvements. Furthermore, there was a lack of sustainability of enterprise resource planning operations, due to excessive reliance on vendors, while system training and the transfer of skills were not prioritised.
- Most auditees did not have automated performance information systems, as also identified in the past four years, but were using Excel spreadsheets to record and report on performance information, which were more susceptible to data manipulation. Adequate performance information systems are key to measuring auditees' service delivery to the public. If information on these systems is not reported accurately and completely, it may have a negative impact on service delivery to the citizens of South Africa.

Evaluation of qualifications and experience of chief information officers or information technology managers

Figure 4 indicates that the **qualifications and experience of the chief information officers or IT managers** in government were adequate at most of the auditees, which meant that they had relevant information and communication technology qualifications and six or more years of relevant experience.

Most of the chief information officers or IT managers at departments and public entities had the qualifications and experience required to implement the IT governance structures and controls that would ensure improvement in the IT controls of government. National departments, the Free State, KwaZulu-Natal, Limpopo, Mpumalanga and the Northern Cape improved from the previous year due to more auditees having chief information officers or IT managers with the required level of qualifications and experience as well as vacancies that were filled, while the Eastern Cape was the only province where all auditees assessed had staff with the relevant qualifications and experience. Where national and provincial auditees employed chief information officers or IT managers with adequate qualifications and experience, it had a positive impact on improved IT controls over the past three years.

The regression in Gauteng, the Western Cape and public entities was mainly due to vacancies in positions that had previously been filled or chief information officers and IT managers with inadequate qualifications.

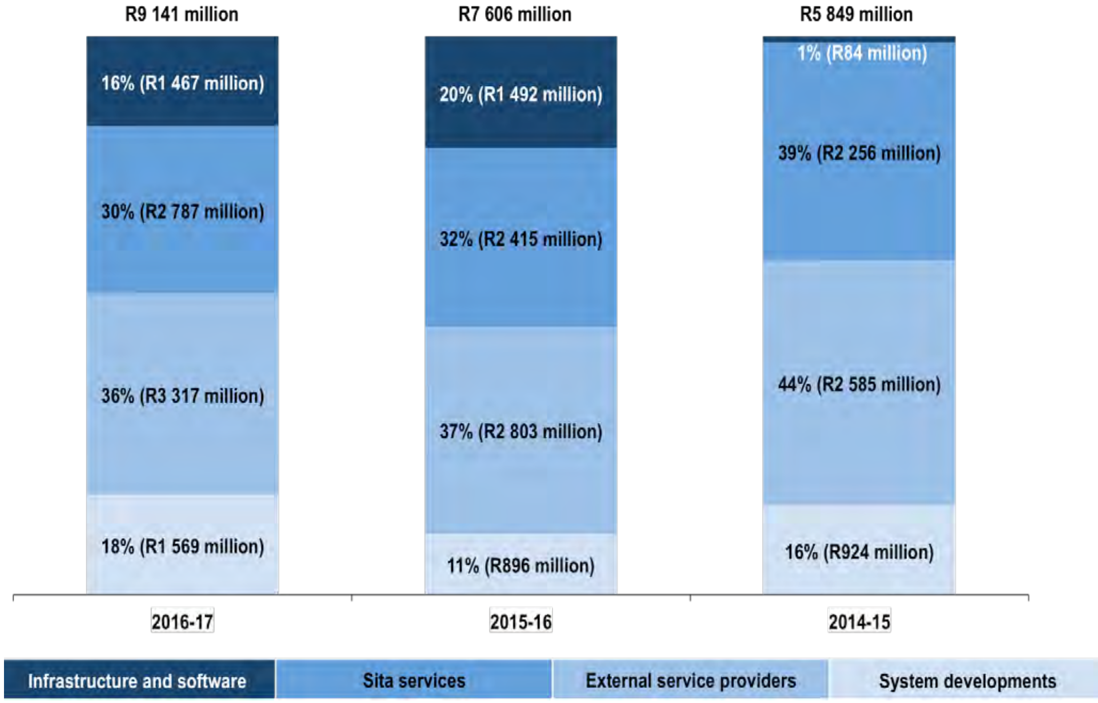
Figure 4: Qualifications and experience – chief information officers or information technology managers

Expenses related to information technology at the provincial and national departments

Figure 5 breaks down the **approximate IT-related expenditure** in terms of **infrastructure and software, Sita services, external service providers** and **system developments**.

IT-related expenditure increased by R3 292 million (56%) in the last two years, with the largest increase in spending being on infrastructure and software as well as system developments, which increased from 1% to 16% and from 16% to 18% of the IT-related expenditure, respectively. This was due to revitalisation and modernisation projects undertaken by some of the key departments and provincial departments to enhance broadband, upgrade internet links, replace ageing servers and install next-generation firewalls. The increase was evident in all the provinces and at national government level. The amounts spent on Sita support services and services rendered by external service providers were more or less equal. Expenditure in this regard did not significantly increase from the previous year but overall represented 66% of the total amount spent – representing the largest part of the IT expenditure. Despite this, we found that the performance monitoring processes of service providers were inadequate. This resulted in payments being made by departments without monitoring whether services were delivered at the agreed upon level of quality, due to the lack of, or inadequate, project management offices within government, as we had also reported previously.

Figure 5: Expenses relating to information technology at national and provincial departments



Large information technology projects currently underway

Integrated financial management system project

The IFMS project, managed by the National Treasury, awarded the contract to replace the ageing transversal financial systems (BAS, Persal and Logis) to Oracle as the only software solution provider in April 2016. Although a project management office was established as reported last year, the contract had been suspended and the responsibilities moved to internal staff of the National Treasury, which now have to come up with a new plan on how this function will be managed. The project governance framework has been formalised and is being implemented. With the appointment of the solution provider, the project aims to implement the revised IFMS solution by 2022, as previously reported.

The roles and responsibilities as reported last year in providing independent assurance were still being formalised between ourselves, the National Treasury, Department of Public Service and Administration (DPSA) and Sita, as the DPSA requires additional clarity on their involvement on the IFMS project before signing off on the IFMS audit strategy and framework. To ensure proper oversight of the project, the National Treasury's internal audit function continues to audit the IFMS project from time to time to highlight possible risks and concerns to management.

We are also focusing on the IFMS programme's contracts and SCM processes through our normal regularity audits at all affected auditees, and reported on this in their reports during the 2016-17 financial period. Concerns included a lack of an approved and detailed project plan indicating milestones by when tasks must be completed and signed off by service providers. Therefore, accountability and consequence management would have been difficult to enforce (**ACT**). There was also no detailed budget per year for the IFMS project, which made it difficult to track and report on the actual expenses relating only to the IFMS – the actual amount spent as at 31 March 2017 could thus not be determined.

Integrated justice system (IJS)

The objective of the IJS programme is to electronically enable and integrate the end-to-end criminal justice business processes. Once fully operational, the IJS will enhance the efficiency and effectiveness of the entire criminal justice process by increasing the probability of the successful investigation, prosecution and punishment for priority crimes and, ultimately, the rehabilitation of offenders.

The IJS programme management office had made great strides in addressing project governance issues identified during the 2015-16 review, but project artefacts were still not in place. Additional issues identified during the 2016-17 review included the inadequate use of prescribed templates and a failure to update project information on the Project Portfolio Office system; the lack of an organisational change readiness report; the absence of key project management artefacts; and the lack of training, organisational change management, and operational support plans. An assessment of the IJS modernisation programme revealed a lack of progress on some of the key project deliverables scheduled for 2016-17, resulting in the shifting of deliverables to the next financial year. Although approved, shifting these timelines will have a negative impact on the overall delivery of the IJS.

Approximately R4,67 billion had been spent on the IJS programme as at 31 March 2016, over a period of more or less 12 years since 2004, against a budget of R4,92 billion as reported by the IJS project management office. In comparison, as at the end of the 2016-17 financial year, spending on the IJS programme was under R5 billion, against a budget of R5,26 billion. The budget spent during the 2016-17 financial year related to progress made in implementing and upgrading IJS-related information systems (such as the electronic case management system, inmate integrated management system, electronic court filing system, and integrated case management system), and infrastructure development and upgrades by the eight IJS member departments.

e-Government, e-Health and e-Education strategies

e-Government

The e-Government strategy is intended to provide a more coordinated and citizen-driven focus to the country's e-Government initiatives, thus ensuring that government brings services closer to citizens through an organised and holistic adoption of information and communication technology. To ensure the successful implementation and effective monitoring by the DPSA of this strategy, the Public Service Regulations of 2016 require that the minimum norms and standards for information and communication technology be developed and monitored by the DPSA.

Therefore, Sita revised the Minimum Interoperability Standards and submitted these to the DPSA. The standards are currently being reviewed by the DPSA's legal services and have not yet been finalised. As the Minimum Information Security Standards remain a contested area, they have been taken out of the revised Public Service Regulations of 2016, as they are believed to fall under the minister of Security. No discussions relating to updating this document took place during the period under review.

The position of government chief information officer in the DPSA had not been filled for more than six years, with acting incumbents dating back to 2011. The lack of stability in this role has had an impact on the timely finalisation and implementation of standards, guides and procedures to be issued to departments. In addition, this had an impact on the improvement of the IT control environment within government, as most departments were still struggling with the implementation of the Corporate Governance Information and Communication Technology Policy Framework.

e-Health

The e-Health Strategy South Africa 2012-16 is aimed at reducing waiting times, improving data quality and integrity, increasing timely access to data, streamlining registers, and strengthening information management in the public health sector.

Little progress had been made with the implementation of this strategy in the provinces, due to budget constraints, IT-critical vacancies and a lack of prioritising the implementation of the initiatives. Provincial health departments had also not been monitoring the e-Health initiatives. In addition, minimal progress had been made regarding the development of information and communication technology infrastructure, network connectivity as well as the integration of systems, with the exception of Gauteng that recently embarked on an information and communication technology infrastructure upgrade.

Two provinces (Limpopo and North West) had still not developed their e-Health strategies, as reported previously, due to senior management not taking accountability to prioritise this initiative. Furthermore, the eHealth strategy was still in draft format in the Eastern Cape as it was only prioritised during 2016-17, while only the Northern Cape had incorporated e-Health initiatives into their approved IT strategy.

All provinces still faced challenges relating to connectivity and interfacing key systems (such as billing, patient registration and pharmaceutical systems), which contributed to the objectives of the e-Health Strategy South Africa 2012-16 not being achieved yet.

e-Education

The White Paper on e-Education (2004) revolves around the use of information and communication technology to accelerate the achievement of national education goals. The main outcome is to increase access to such technology to support curriculum delivery and improve learner attainment.

The Department of Basic Education has continuously been monitoring the measures put in place to accelerate the achievement of e-Education in South African schools, which include deliverables and activities such as electronic content resource development and distribution; professional information and communication technology development for management, teaching and learning; and access to information and communication technology infrastructure and connectivity.

In previous years, four provinces had delayed the implementation of this white paper due to challenges around the availability of budgets at provincial level, inadequate broadband infrastructure especially in rural areas, and teachers' limited capability to use information and communication technology.
However, during the 2016-17 financial period, Limpopo developed a strategy that was aligned to the white paper that drives the initiatives of e-Education. Two provinces (Eastern Cape and North West) had started with the development of e-Education strategies, which still had to be approved. Only the Northern Cape had not started developing e-Education strategies, as resources have not yet been allocated to this initiative.

In addition, due to the slow movement and lack of skills in some provinces, the department rolled out the operation phakisa initiatives as an implementation plan to all the provinces and different role players to assist in the information and communication technology education rollout plan.

Inadequate progress and a lack of monitoring and prioritisation by senior management in the provinces could result in the e-Education strategy not being implemented, thus ultimately hampering the achievement of quality education in the country.

Most common root causes

Most of the common root causes remained the same as in the past four years, demonstrating a lack of accountability by those who had to ensure that decisions and actions were implemented and that consequence management was enforced. The most common root causes remained the following:

- Although the **skills and experience** in departments and public entities were adequate at **chief information officer or IT manager level,** with only 5% of these positions being vacant at year-end, auditees could not attract staff to fill vacant key positions such as those of system controllers and information security officers. Furthermore, some IT divisions did not operate on a strategic level to influence the design and implementation of adequate policies and procedures.

- The **chief information officers, IT managers and IT staff** did not fulfil their **responsibilities** by ensuring compliance with the controls established to secure and regulate their departments' IT environments, due to a lack of consequence management.
- The **accounting officers and accounting authorities** did not prioritise the **approval of IT policies and procedures** to ensure that proper internal controls existed and could be enforced.
- The **performance monitoring processes of IT service providers** were not adequately enforced to ensure that services were rendered at the agreed level of quality or standard.
- Most departments were fixing **symptoms** rather than implementing improved IT controls. Another major concern was the ineffectiveness of **those charged with governance**, as they were not proactive in addressing the audit findings and preventing recurrences.
- The replacement of outdated infrastructure and software to improve IT controls was hindered by **insufficient funding**. Although there was a significant increase in spending over the last two years due to a few key departments that were modernising, it may take a few years to address the backlog of outdated infrastructure and software that currently exists in government.

Conclusion

As the majority of financial management controls are automated and monitoring takes place mostly on reports generated by the IT systems, good IT controls and skills are fundamental to enabling robust financial management systems (**DO**) and in-year monitoring (**CHECK**).

13 Assurance providers

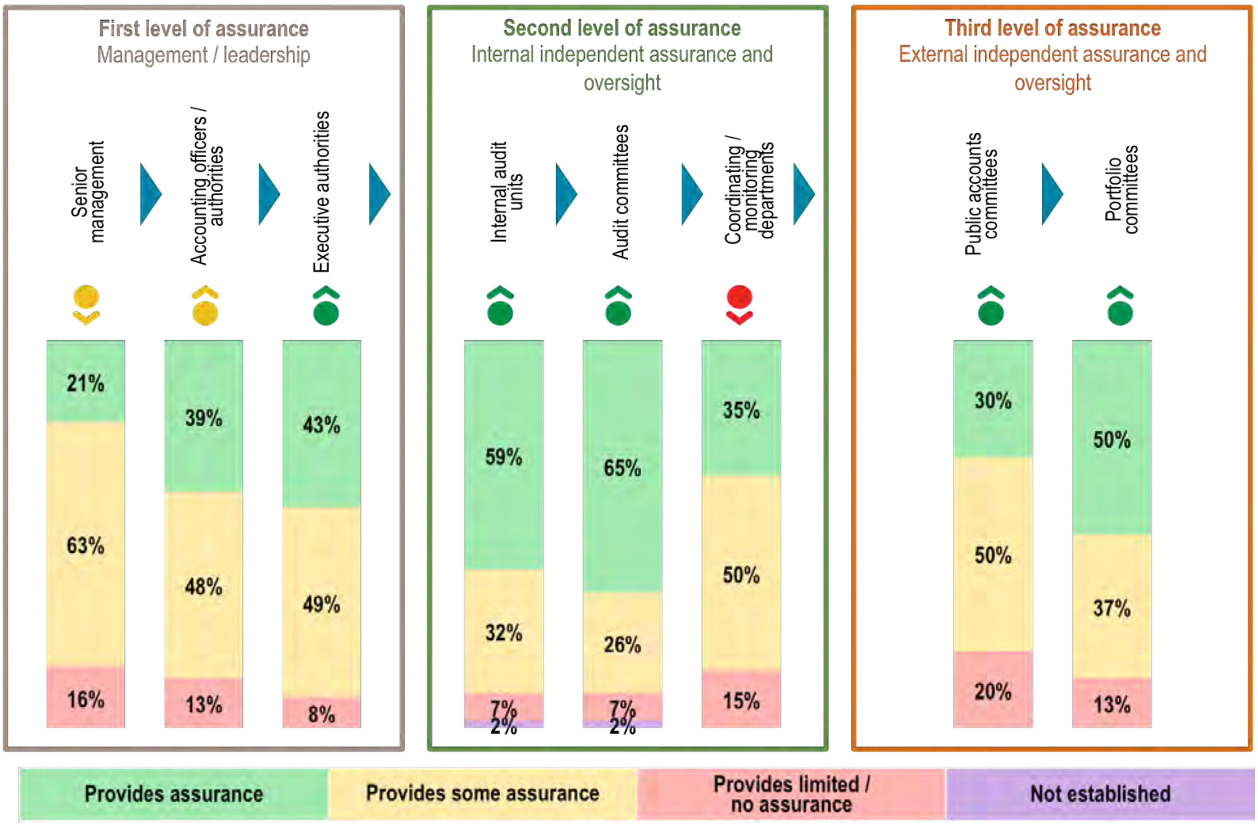
13. Assurance providers

Accounting officers and authorities use the **annual report to report on government spending and how they performed against the targets** set for the year, while one of the important functions of public accounts committees, portfolio committees and other oversight structures is to consider these annual reports and ensure that there is accountability for the results.

To perform their oversight function, they need **assurance that the information in the annual report is credible**. To this end, the annual report also includes our audit report, which provides assurance on the credibility of the financial statements, the performance report and the auditee's compliance with legislation. Our reporting and the oversight processes reflect on history, as they take place after the financial year. Many other role players contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.

Figure 1 shows our assessment in 2016-17 of the **assurance** provided by the management or leadership of auditees and those that provide independent assurance and oversight. The arrows show the movement in assurance levels since 2013-14. We determined the movements by taking into account either increases in 'provides assurance' or reductions in 'provides limited/no assurance'.

Figure 1: Assurance provided by key role players



The assurance provided by five of the key role players had improved since 2013-14, with a slight improvement in the assurance provided by the accounting officers or authorities. There was a regression in the assurance provided by the coordinating or monitoring departments and a slight regression in the assurance provided by senior management.

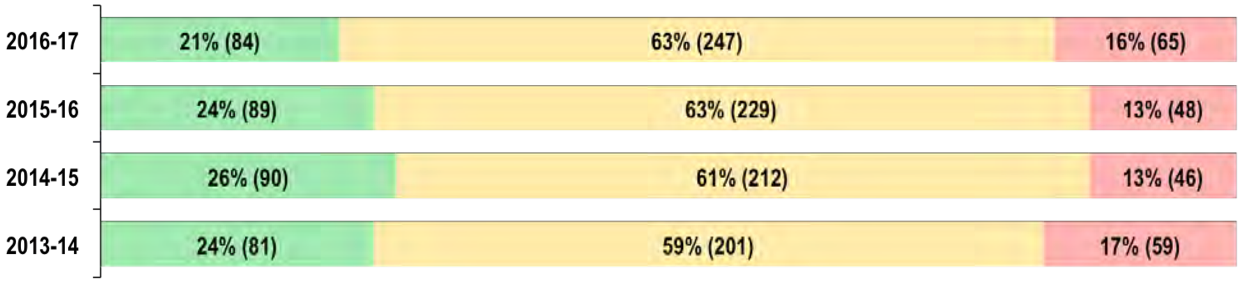
Low levels of assurance show that there are weaknesses in this crucial element of the improvement cycle, being monitoring to ensure that internal controls are adhered to, risks are managed and outcomes are achieved.

We provide an overview of the level of assurance provided by the different role players in the rest of this section. Please refer to section 17 for further detail on the role of each role player providing assurance and the assessment thereof. We also reflect on the status of commitments made (whether honoured or not) and key initiatives to be undertaken by the treasuries, offices of the premier, the Department of Planning, Monitoring and Evaluation (DPME), and the DPSA.

The following legend applies to the figures shown:

Provides assurance	Provides some assurance	Provides limited/no assurance	Not established

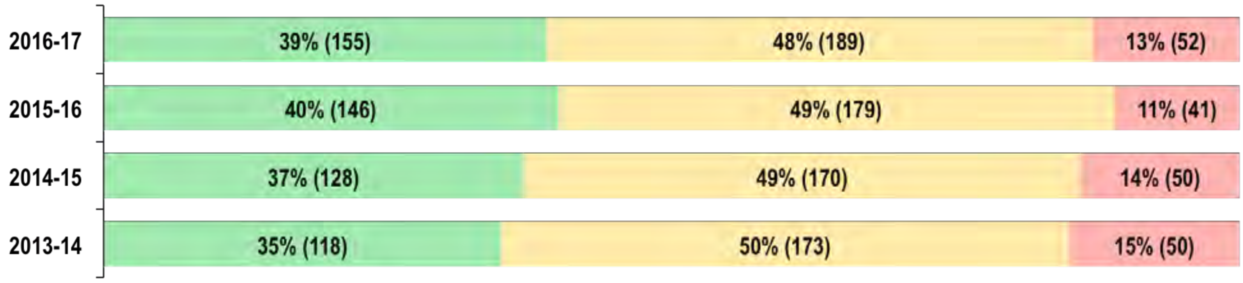
Senior management



Accounting officers, chief executive officers and executive authorities rely on senior management, which includes the chief financial officer, chief information officer, head of the SCM unit and those responsible for strategic planning and monitoring, to implement basic financial and performance management controls. However, the assurance provided by senior management remained the lowest of all the assurance providers. Senior management at 79% of the auditees did not provide the required level of assurance in 2016-17 – a slight regression compared to the 76% in the previous year and in 2013-14. The number of auditees at which senior management provided limited or no assurance increased slightly.

At some auditees, instability and vacancies in senior management positions and a lack of skills in the finance units reduced the effectiveness of senior management, but these problems were no longer widespread at departments and public entities, as detailed in section 11. Although senior management ensured that policies and procedures were in place at most auditees, compliance with such policies and procedures as well as with legislation was not reviewed and monitored. Similarly, action plans were in place at most auditees to address audit findings but again the implementation (**DO**) and monitoring thereof (**CHECK**) were the parts of the process that were not in place. The poor quality of the financial statements and performance reports submitted to us for auditing is testament to the inability of senior management to give credible assurance to their accounting officers on the reports they produce. Often we see accounting officers not holding senior management to account for the poor submissions (**ACT**) – especially if the final audit outcome is positive as a result of us identifying the misstatements and allowing them to make the adjustments.

Accounting officers or authorities



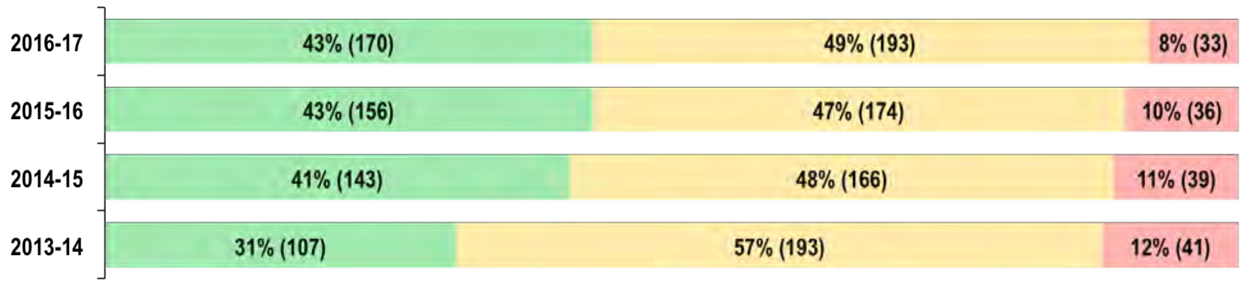
The responsibilities of accounting officers and authorities are clearly described in section 38 (for departments) and section 51 (for public entities) of the PFMA. In our assessment, however, accounting officers or authorities at 61% of the auditees were still not providing the required level of assurance by 2016-17.

Instability at board level and vacancies in the chief executive officer position negatively affected the assurance provided at some public entities, as detailed in sections 4 and 11. Accounting officers and authorities were often hampered in the performance of their responsibilities, as they did not receive credible financial and non-financial information from their senior management – but then, they also did not always address this weakness. The accountability process is weakened by not ensuring that senior management members account for their results and actions, and by not consistently applying consequence management for poor performance and transgressions.

Accounting officers and authorities must ensure that a strong control environment is in place at auditees. Unfortunately at some auditees, they were creating hurdles by not approving policies, delaying decisions or not ensuring that audit action plans, internal audit findings and resolutions from oversight committees were prioritised.

The assurance provided by accounting officers or authorities slightly improved over the past four years. The number of auditees at which they provided sufficient assurance had increased since the previous year (the percentage shows a regression, but it is as a result of the increase in the number of auditees being audited since 2015-16).

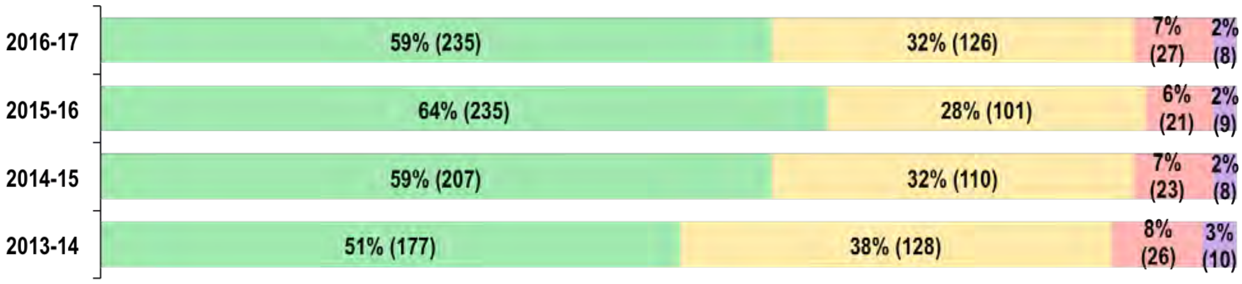
Executive authorities



The executive authorities (ministers and members of the executive councils) have a monitoring and oversight role in their portfolios and play a direct role at departments, as they have specific oversight responsibilities towards their departments in terms of the PFMA and the Public Service Act. They are well placed to bring about improvements in the audit outcomes by becoming more actively involved in key governance matters and by managing the performance of the accounting officers and authorities.

Our assessment that executive authorities, while improving over the past four years and slightly improving from the previous year, are not yet providing the required level of assurance is based on the inadequate leadership controls observed at 50% of the auditees, as detailed in section 10. It is further supported by our assessment of the impact that they have had on audit outcomes as observed through our regular interactions with them and the commitments they had made and honoured to improve audit outcomes.

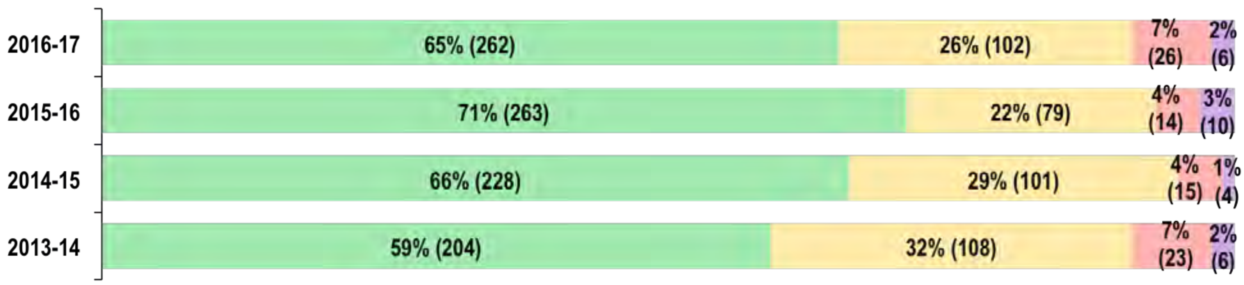
Internal audit units



Internal audit units were in place at all but eight auditees by 2016-17. A total of 59% of the internal audit units provided assurance, which was an improvement from the 51% in 2013-14. The number providing assurance remained the same as in the previous year (the percentage shows a regression, but it is as a result of the increase in the number of auditees being audited since 2015-16).

At most auditees, well-resourced and effective internal audit units have helped to improve internal controls and have had a positive impact on audit outcomes. We assessed that 249 of the internal audit units (2015-16: 244) had a positive impact on audit outcomes. The main reason for a lack of positive impact was the failure by management to address internal audit findings.

Audit committees

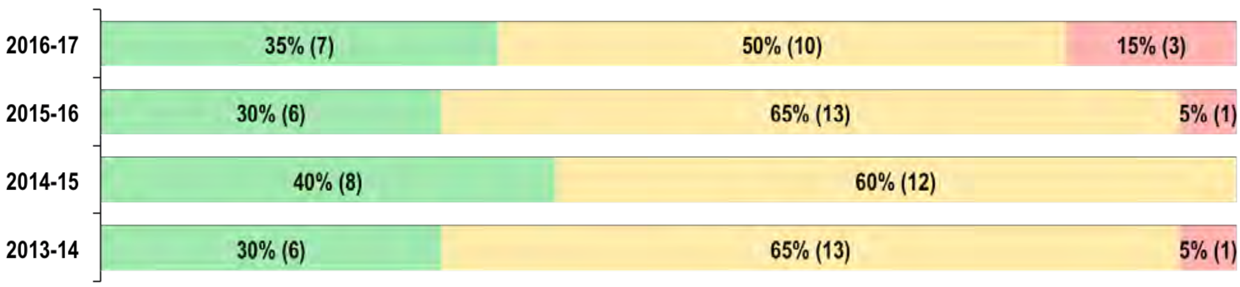


At 65% of the auditees, audit committees provided assurance, which was an improvement from the 59% in 2013-14 but slightly fewer than the number in 2015-16.

We assessed that the audit committees of 304 of the auditees had a positive impact on the audit outcomes (2015-16: 284). The number of audit committees that interacted with the executive authorities had also increased to 353 from 321 in 2015-16.

We are concerned, however, that at some auditees the audit committees championed the view of management against the auditor without fully understanding or interrogating the facts. Audit committees should ensure that management fulfils its responsibilities. Committee members should remain independent and fully apply their knowledge and experience in fulfilling their very important assurance role.

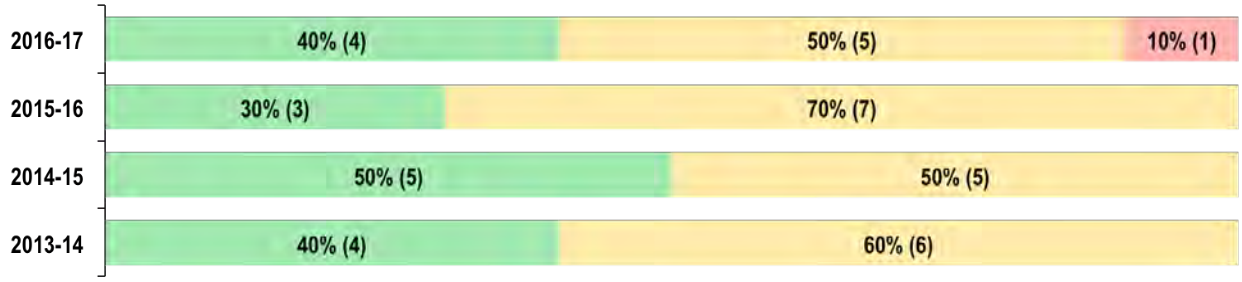
Treasuries, offices of the premier and Department of Planning, Monitoring and Evaluation (coordinating/monitoring departments)



Some departments play a coordinating and monitoring role at national and provincial level as defined in legislation and in their mandates, which should contribute to the overall assurance process. These departments are the offices of the premier, provincial treasuries, the National Treasury and the DPME. We assessed the impact of these departments on the controls of the auditees based on our interactions with them, commitments given and honoured, and the effect of their actions and initiatives.

In our assessment, most of these departments provided some assurance through their coordinating and monitoring functions. Although some departments improved over the four years, there were also some regressions. We summarise our assessments below, but provide a more detailed view on the provincial role players in section 16. We also touch on the role of the DPSA although we did not assess them as an assurance provider.

Provincial treasuries and the National Treasury



The assurance provided by the treasuries regressed over the four years. The provincial treasuries in Gauteng, the Northern Cape and the Western Cape consistently provided assurance over the past four years, but the assurance regressed from 2015-16 in the Free State with the provincial treasury only providing some assurance, and in North West where the provincial treasury provided limited or no assurance in 2016-17. Only the provincial treasury in the Eastern Cape improved from the previous year by providing full assurance in 2016-17.

We assessed the remaining provincial treasuries and the National Treasury as providing some assurance.

Table 1 lists the commitments previously made by the treasuries to improve audit outcomes and the status thereof, while table 2 lists the key initiatives agreed on by them in response to the current year's audit outcomes.

Table 1: Status of previous commitments

Number	Previous year's commitments	National Treasury	Provinces								
			EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	The continued roll-out of financial management products as well as capacity building in the whole of government remains a priority.										
2	Although a number of support plans have been developed to assist targeted departments and entities in financial distress, continue to provide support to address financial management weaknesses.										
3	Procurement reform: Following the SCM initiatives from the previous year, transforming government procurement to make it more cost-effective, transparent and equitable remains an area of significant importance.										

Number	Previous year's commitments	National Treasury	Provinces								
			EC	FS	GP	KZN	LP	MP	NC	NW	WC
4	Overhauling SCM systems: Ensure a simplified and modernised SCM environment in government in response to SCM initiatives and the review of SCM policies.										
5	Focus on reducing irregular expenditure caused by SCM non-compliance.										
6	Enforce consequences for those that incur irregular expenditure.										
7	Maintain appropriate records to support credible performance and financial reporting.										
8	Continue to support the delegated local municipalities in the province within the legislative confines of the role of the provincial treasury. This may, among others, be through the current intergovernmental relations structures in the province, e.g. the chief financial officers forum, debt management committee, grant management committee, and engagement forum of members of the executive council / members of the mayoral committee.										
9	Enhance the review of quarterly financial statements, including disclosure notes, supporting schedules and key reconciliations; and provide feedback to the departments and audit committees to maintain unqualified financial audit outcomes for all provincial departments and entities.										
10	Address the non-compliance with SCM Regulations to prevent irregular expenditure.										
11	Reduce the unauthorised expenditure in the province.										
12	Section 18 intervention: Financial management resuscitation plan – improved cooperation between seconded officials of the provincial treasury and departmental officials.										
13	Establish an independent panel to deal with consequence management in the province. The panel will consist of different experts from fields such as labour relations, law and human resources. This is to ensure that the committee is fully equipped to effectively deal with consequence management.										
14	Collaborate with the National Treasury and Local Government and Human Settlements on the appropriate accounting framework for the compilation of the outstanding financial statements of the tribal authorities in the province.										

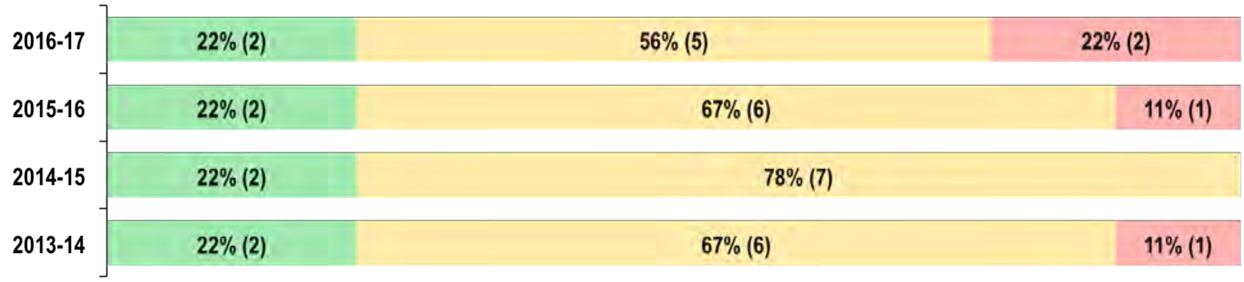
Number	Previous year's commitments	National Treasury	Provinces								
			EC	FS	GP	KZN	LP	MP	NC	NW	WC
15	In addition to supporting the commitments of the premier, recommitted to continue support and guidance through budgetary control, monitoring of monthly reports and enforcement of financial management practices. It is pleasing to note that these initiatives contributed to the province not incurring unauthorised expenditure for the fifth consecutive year.										

Completed **In progress**

Table 2: Key initiatives agreed on

Number	Key initiatives	National Treasury	Provinces								
			EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	Procurement reform: Transforming government procurement to make it more cost-effective, transparent and equitable remains an area of significant importance.										
2	Governance monitoring and compliance: (i) Provide continued support to the academic support programme for prospective chartered accountants. (ii) Issue guidelines to assist with the effective implementation of the revised Treasury Regulations.										
3	Exercise oversight over state-owned companies.										
4	Budget reforms for provincial public entities.										
5	Assist Education to reduce its qualification areas.										
6	Provide support to Health and Education as they have the biggest budgets.										
7	Address the challenge of accruals across all departments.										
8	Monitor and address the shortcomings identified during the early implementation stages of the open tender process.										
9	Exercise oversight over SCM with the aim of reducing irregular expenditure and ensuring effective and efficient procurement spending.										
10	Hold bilateral meetings with the AGSA to discuss any issues arising from both provincial and local government audits.										

Offices of the premier



The nine offices of the premier are responsible for specific coordinating functions and the provision of strategic direction within their respective provinces. Our assessment of assurance is based on the actions taken by them and the support provided to the provincial departments and public entities to achieve good governance and clean administration in their provinces.

The assurance provided by most offices of the premier was similar to the previous years. The most notable exception was in North West, where the assurance provided regressed from some assurance in 2015-16 to limited assurance in 2016-17. The premier's office in the Free State also provided limited or no assurance in both 2015-16 and 2016-17. In both these provinces, the impact of the inadequate direction and failure to honour commitments made to improve audit outcomes can be seen in the deteriorating results of the provinces.

As in previous years, the offices of the premier in Gauteng and the Western Cape were the only ones that provided the desired level of assurance. The tone set by these premiers and their commitment to accountability are reflected in the continued good results of the provinces.

Table 3 lists the commitments previously made by the offices of the premier to improve audit outcomes and the status thereof, while table 4 lists the key initiatives agreed on by them in response to the current year's audit outcomes.

Table 3: Status of previous commitments

Number	Previous year's commitments	Provinces								
		EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	Appoint a permanent head of department for Education.									
2	Fill other critical vacant posts at Education.									
3	Resolve disputes raised on 2015-16 audit reports.									
4	Review the use of implementing agents with a view to eliminating this practice.									
5	Accounting officers to provide more assurance through oversight and taking ownership of the control environment.									
6	Honoured the commitment to fast-track the implementation of the open tender process to assist in curbing irregular expenditure. Will continue to monitor the implementation of the open tender system to encourage transparency and accountability regarding procurement and contract management, with the aim to get it gazetted through the provincial legislature.									
7	Monitor implementation of the transformation, modernisation and reindustrialisation plan through the different departments' annual performance plans and quarterly reporting.									
8	Address the root causes of poor audit outcomes.									

Number	Previous year's commitments	Provinces								
		EC	FS	GP	KZN	LP	MP	NC	NW	WC
9	Fill vacancies in key positions, notably those of accounting officers.					In progress				
10	No more disclaimers. If there are disclaimers, there will be serious consequences for officials as well as for political leaders.					Completed				
11	Continuously refine involvement in monitoring and guiding provincial departments through the monitoring and evaluation unit.						Not implemented			
12	Executive authorities to receive monthly reports on the performance of their departments, particularly regarding payments within 30 days and SCM compliance.						In progress			
13	Ensure that the required human capital is appointed at Environment so that the department is able to run smoothly.							Completed		
14	Ensure that the quality of financial statements improve.							In progress		
15	Cabinet to continue to engage with heads of departments and chief financial officers to proactively resolve financial and SCM issues.							In progress		
16	Establish a committee consisting of the head of department: Finance, Office of the Accountant-General, a legal representative from the premier's office and an external chartered accountant to guide the process to address unauthorised, irregular and fruitless and wasteful expenditure and also to ensure a uniform interpretation of regulations governing the treatment of such expenditure. Resolutions taken by the committee will be communicated via a treasury circular.								In progress	
17	The premier to continue using the premier's coordinating forum to coordinate and monitor provincial oversight, as well as interactions with members of the executive council, on a monthly basis to determine what progress had been made towards clean administration. This commitment is further underpinned by strategic goal 5 of the provincial strategic plan for 2014-19, which specifically outlines the provincial government's commitment to embedding good governance and integrated service delivery through partnerships and spatial alignment.									Completed
18	The provincial executive has recommitted to ensuring that operation clean audit, coordinated by the ministries of provincial treasury and local government (Troika), will remain a standing agenda item of the premier's coordinating forum for monitoring and evaluation of municipalities' key controls and commitments, as well as sharing best practices to achieve sustainable clean audit outcomes.									Completed

Completed | **In progress** | **Not implemented**

Table 4: Key initiatives agreed on

Number	Key initiatives	Provinces								
		EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	Ensure that accountability is enforced and that the assurance provided by accounting officers and senior management improves.									
2	The province will find a way to deal with medical legal claims in the absence of a national response.									
3	At least 50% of departments to achieve a clean audit status in 2017-18.									
4	Reduce irregular expenditure caused by SCM non-compliance and monitor implementation of consequence management.									
5	Finalise the matter of classification of expenditure between goods and services and transfer payments (even if a declaratory order from court must be obtained).									
6	Heads of departments to implement consequence management for transgressions.									
7	Continue oversight and acceleration of provincial initiatives for the achievement of clean administration across the province. Obtain 75% clean audits in the 2017-18 financial year.									
8	Action plans on audit outcomes to be a standing item at head of department forum meetings, with progress to be reported by heads of departments and escalated to the cabinet lekgotla. Implement a checklist to track this at head of department level.									
9	Members of the executive council to spend more time on providing oversight of departments.									
10	The director-general to ensure that the operation clean audit structure is revived in the province.									
11	Leadership and senior management to deal with issues relating to irregular expenditure and performance reporting.									
12	Departments to ensure that they have quarterly engagements with the AGSA, similar to those with the premier's office, so that issues are dealt with during the course of the year.									
13	The provincial treasury to validate the current status of public entities and to communicate the closing of entities and other changes appropriately by November 2017 to key role players.									
14	The provincial treasury to submit the 2018-19 annual performance plan for departments to the AGSA by 15 December 2017; and ensure that the submissions for the oversight process are aligned to legislation.									

Department of Planning, Monitoring and Evaluation

We assessed that the DPME had provided the required level of assurance since 2014-15 – an improvement from the some assurance provided in 2013-14. The department provided support and guided planning processes in government by using a range of planning frameworks, including the regulatory frameworks for strategic plans, annual performance plans and programme plans. They also reviewed the annual performance plans of national and provincial departments to contribute to the quality of the plans. However, not all departments implemented the DPME's recommendations.

Table 5 lists the commitments previously made by the DPME to improve audit outcomes and the status thereof, while table 6 lists the key initiatives agreed on by them in response to the current year's audit outcomes.

Table 5: Status of previous commitments

Number	Previous year's commitments	
1	Monitor and report on the 30-day payment commitment.	
2	Ensure that sector plans for strategic sectors are developed and implemented.	
3	Monitor the performance and effectiveness of SOEs in directing their resources towards the country's development goals and objectives.	
4	Align national budget to key priorities.	

Completed	In progress

Table 6: Key initiatives agreed on

Number	Key initiatives	
1	Develop enabling legislation for planning, monitoring and evaluation.	

In progress

Department of Public Service and Administration

Although the DPSA does not provide direct assurance, they play an important role in improving the management of HR and IT in government.

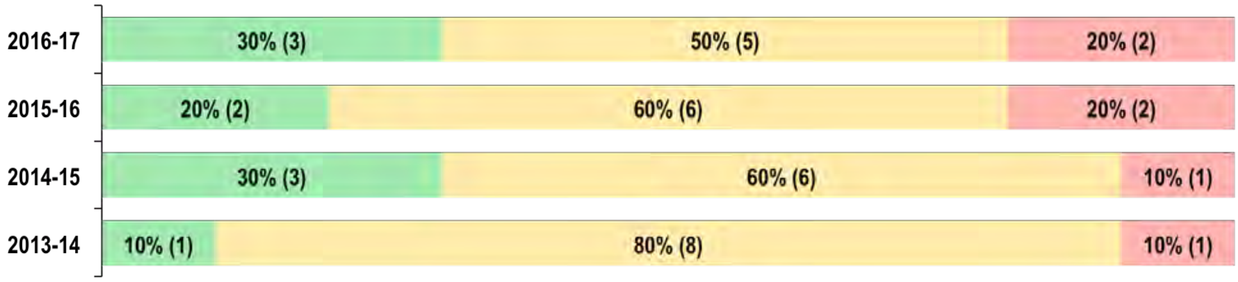
Table 7 lists the commitments previously made by the DPSA to improve audit outcomes and the status thereof. At the time of this report, no key initiatives had been agreed on by them in response to the current year's audit outcomes.

Table 7: Status of previous commitments

Number	Previous year's commitments	
1	The amended Public Service Regulations issued in terms of the Public Service Act became effective on 1 August 2016, which further regulate the employment relationship of government employees that do business with organs of state.	
2	Turnaround time to resolve disciplinary cases at national and provincial departments.	
3	Approval of a mentoring and peer support framework that seeks to enable individuals to develop through the transfer of knowledge and skills from peers.	
4	The competencies of financial management, people management and empowerment still required attention in government.	
5	The usage of the e-Disclosure system for financial disclosures.	
6	Self-assessment of HR compliance in the management performance assessment tool to monitor compliance with the HR and information and communication technology governance framework by individual departments.	
7	Letters issued to other ministers highlighting areas of non-compliance with the Public Service Act and regulations as provided for in section 16A of the Public Service Act.	
8	Directive on compulsory capacity development, mandatory training days and minimum entry requirements for government.	
9	Filling the position of the government chief information officer.	
10	Lack of adequate understanding and involvement in the strategic alignment of business strategies against IT-driven initiatives by the majority of government IT officers.	
11	Minimum Interoperability Standards and Minimum Information Security Standards were not approved and revised accordingly.	

Completed	In progress	Not implemented

National Standing Committee on Public Accounts (Scopa) and provincial public accounts committees



We assessed that 30% of the public accounts committees provided the required level of assurance – with Scopa as well as the committees in the Eastern Cape and the Western Cape providing full assurance. Only two public accounts committees were assessed as providing limited or no assurance – those in the Free State and North West. The rest of the public accounts committees provided some assurance during 2016-17.

National Standing Committee on Public Accounts

Scopa has a responsibility to oversee the expenditure of public funds. They use various mechanisms to discharge their oversight responsibilities, including the following:

- Utilising insights provided by us during briefings before public hearings and oversight visits to departments.
- Conducting hearings in the presence of the Anti-Corruption Task Team and Hawks to ensure that prolonged and suspicious cases are handed over to them.
- Requesting progress reports from the Special Investigating Unit on investigations into cases of corruption.

Scopa provided the required level of assurance during the year under review and further improved their oversight approach. The following were notable areas in this regard:

- With regard to their anti-corruption stance and maladministration, the focus was on departments that incurred irregular and fruitless and wasteful expenditure, conflict of interest, departments that failed to table their annual reports on time, and any other occurrences where losses of public funds were identified.
- A few oversight visits were conducted and the engagements with stakeholders were meaningful by elevating the importance of consequence management. Scopa further pursued individual departments where there was evidence of disregard for consequences.
- Ties with the Office of the Chief Procurement Officer were strengthened by holding quarterly engagements to keep the committee updated on irregularities in the public sector, especially relating to SCM and the non-payment of invoices within the prescribed time.
- The committee continued to intensify their focus on, and advocate for the importance of, accountability as per the combined assurance model and section 38 of the PFMA.

The intense effort of Scopa resulted in members of the general public acknowledging our reports, which increasingly gained publicity and recognition from them.

The committee still needs to advocate for an opportunity to debate its reports in the House. Unfortunately no resolutions have been processed yet, which makes it difficult for us to assist the committee in following up on recommendations made.

Provincial public accounts committees

Provincial public accounts committees continued the level of oversight exhibited in the previous year. However, when compared to Scopa, these oversight committees did not sufficiently engage on topical issues in the public space. They still seemed to focus on the elementary elements of oversight without a heightened level of oversight on transversal issues. There was also a lack of coherence in the oversight function of public accounts committees in the provinces. The following are some of the more notable concerns:

- Most committees did not strongly advocate for consequences from their respective executive authorities to address transgressions identified in their administration.
- Some could not facilitate oversight leverage on our findings relating to unauthorised, irregular and fruitless and wasteful expenditure.
- Some committees did not adequately plan their oversight activities to maximise their focus on key issues we have raised.
- The committees did not effectively utilise the media to create the necessary hype and public interest in their oversight activities.
- Although there have been numerous opportunities to take oversight lead on governance failures in the provincial government, committees were unable to take advantage of such opportunities that would have enabled them to build public trust.

Generally, most provincial public accounts committees seemed to struggle with effectively discharging their oversight functions – mostly because of the lack of political will. In instances where they were able to execute their mandate, they were generally hampered by the lack of action and adequate monitoring of their resolutions. The public accounts committee in Limpopo is one of the committees that encountered challenges which hampered effective oversight. For example, most departments demonstrated a lack of respect towards the committee by coming to hearings unprepared. Having said that, public accounts committees in other provinces such as Gauteng, KwaZulu-Natal and Mpumalanga could sufficiently discharge their responsibilities and were able to hold successful hearings.

National and provincial portfolio committees

We assessed that 50% of the portfolio committees provided the required level of assurance – most prominently the national portfolio committees and the portfolio committees in the Western Cape. Only 13% were assessed as providing limited or no assurance – most prominently the portfolio committees in North West and the Free State. The rest of the portfolio committees provided some assurance during 2016-17.

National portfolio committees

Portfolio committees are mandated to oversee executive action on matters relating to policy and service delivery implementation. They play an in-year monitoring role that allows them to take immediate action where there are notable failures. In the recent past, national portfolio committees have effectively executed their mandate. We highlight the following successes in the year under review:

- Since the inception of the ad hoc committee of enquiry on the functioning of the SABC board, there has been a notable vigour from portfolio committees to pursue matters related to the functioning of SOE boards.

- A notable development was that portfolio committees asked relevant questions to departments especially on service delivery issues – particular focus was on the achievement of targets set in departmental annual performance plans.
- Most committees increasingly expressed concerns about the instability of leadership in entities and departments, particularly vacancies in key positions such as chief financial officer and heads of key programmes as set out in the annual performance plans.
- Most committees covered issues raised by the media as informed by the messages in our general reports, such as irregular expenditure.
- Most committees also demonstrated an improved understanding of our mandate; in the past, committees used to ask us what we have done when there was no movement in the audit outcomes.
- Owing to the insight we provided, most committees called on departments to provide regular updates on the actions taken to implement our recommendations.
- The relevant committees provided us an opportunity to share the findings of the performance audit on water infrastructure. The committees were encouraged and receptively acknowledged the findings of the report and committed to hold oversight hearings with the departments concerned.

While there was a general positive trend in the assurance provided by portfolio committees, the following issues still require attention:

- While portfolio committees have improved their oversight activities, a few committee members still did not adequately understand our mandate – as illustrated by confusion around the accountability for negative audit outcomes.
- The rotation of chairpersons owing to executive and other reshuffling hampered the continuation of expertise, particularly in committees identified in our stakeholder interaction plan.

Provincial portfolio committees

The engagements of provincial portfolio committees grew steadily from previous years. However, certain provinces such as North West continued to experience challenges in engaging portfolio committees because of the unavailability of stakeholders due to conflicting priorities, a lack of proper stakeholder relations, and a poor understanding of stakeholder dynamics, among other reasons.

Efforts by several of our internal business units to engage with provincial portfolio committees on our new audit methodology, the status of records reviews and the assessment of portfolio committees yielded some positive results. There was a general appreciation of our value-add to the public sector through these interventions. Most committees demonstrated a willingness to make themselves available to engage with us on key accountability issues. Continual engagements of the provincial portfolio committees are required to see a marked change in the level of oversight they provide.

Association of Public Accounts Committees (Apac)

Apac continued to enhance the capacity of all public accounts committees and portfolio committees through their decentralised training programmes. The portfolio committees that were targeted were education, finance, health, local government and public works. During these programmes, members were exposed to the audit of predetermined objectives as well as performance audit insights. Members were taken through recently published performance audit reports on urban renewal, water infrastructure and pharmaceuticals. Members were quite appreciative of the insights and understanding gained from these engagements.

During the auditor-general's recent PFMA roadshow to Apac's council of delegates, a sense of vibrancy took over the meeting. For the first time, members were vulnerable enough to deal with issues that were deterrents to effective oversight. Members accepted that the reason why there has not been a dramatic improvement in the performance of the public sector was because they have not done their part as oversight. This was primarily because in the past those who had passionately dealt with their oversight responsibilities had fallen victim to reshuffling or expulsion. During the meeting, there was a strong commitment to effective oversight irrespective of the consequences, and members acknowledged that there was a greater prize to be gained from being principled. A call was made to go back to the basics of oversight by embracing the attitude of doing real oversight without fear, favour or prejudice.

Over and above this pledge, the following commitments were made:

- Apac will continue with capacity-building programmes for public accounts committees and portfolio committees.
- All public accounts committees must prioritise a transversal approach in scrutinising the work of auditees with regard to the highlighted areas. In this way, public accounts committees can focus on specific matters at the same time.
- The implementation of our recommendations by auditees must be tracked and monitored throughout the year to ensure that oversight bodies are fully aware of the state of affairs when the processing of annual reports begins. Each department appearing before a public accounts committee must produce an action list every quarter to demonstrate progress towards addressing the issues we have raised. If they fail to do so, they must be sent back.
- There must be closer coordination with portfolio committees to enhance oversight practices. This would ensure that there is continual oversight where portfolio committees pick up on issues raised by public accounts committees to ensure stronger oversight.
- Oversight committees must ensure that accounting officers and executive authorities are held accountable for consequence management.
- Apac must lobby relevant bodies regarding the qualification of SCM professionals and the state of ethics in that profession.

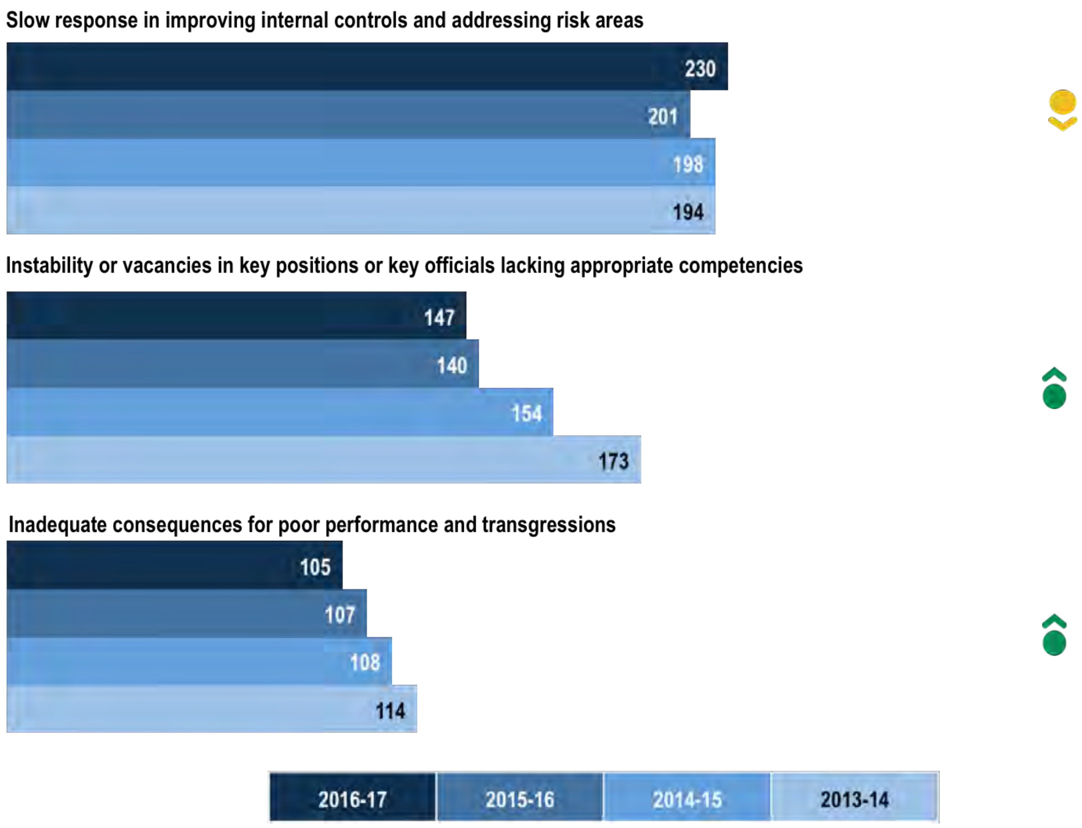
14 Root causes

14. Root causes

Our message on the main root causes of auditees' continuing inability to improve internal controls and obtain better audit results has remained constant over the years.

Figure 1 shows the progress made by auditees in addressing these root causes over the past four years.

Figure 1: Status of overall root causes



There has been little improvement in the response by the leadership to the recommendations we have made, but there has been an improvement in the other two root causes.

Slow response in improving internal controls and addressing risk areas

The most common root cause was that management (accounting officers and senior management), executive authorities and oversight structures (Scopa, provincial public accounts committees and portfolio committees) **did not respond with the required urgency** to our messages about addressing risks and improving internal controls. In our assessment, the slow response was prevalent at both departments (88%) and public entities (83%), having become more widespread at the latter, resulting in the overall increase of this particular root cause.

As mentioned above, our message and its delivery have been consistent for a number of years, but the slow response to this message and to the initiatives taken by national and provincial government is standing in the way of improvements in audit outcomes.

The **main reasons for the slow response** in 2016-17 were the following:

- Audits are often seen as an annual hurdle that should be overcome and our recommendations are not attended to until we return to audit.

- The implementation of commitments made by executive authorities and accounting officers remains a concern. We believe an improvement in the audit outcomes is possible if oversight structures track these commitments and frequently require the leadership to account for the progress made.
- Regarding auditees with audit action plans, some focused on the short term – to only fix the problems that resulted in audit report findings. Sustainable processes are not put in place to ensure that the underlying records do not contain errors, while some auditees are still not getting the full benefit from the financial statement and performance report reviews by internal audit units and audit committees.
- Auditees continued to rely on auditors to assist them at year-end to fix the financial statements and the performance reports. At some auditees, there was little motivation to improve their capacity in this regard.

Instability or vacancies in key positions or key officials lacking appropriate competencies

In our assessment, instability and vacancies in key positions as well as key officials lacking appropriate competencies was a root cause at 54% of the 270 auditees that did not obtain clean audit opinions.

As discussed in section 11, the area of instability and vacancies in key positions has improved, but its impact as well as key officials lacking appropriate competencies was still affecting audit outcomes at 55% of the departments and to a lesser degree at 54% of the public entities.

Inadequate consequences for poor performance and transgressions

As reported in section 9.3, there were weaknesses in the consequence management of just over a third of the auditees. These weaknesses contributed to poor audit outcomes at 39% of the auditees that did not obtain clean audit opinions.

It is important that officials who deliberately or negligently ignore their duties and contravene legislation should be dealt with decisively through performance management and by enforcing the legislated consequences for transgressions. If they are not held accountable for their actions, the perception is created that such behaviour and its results are acceptable and tolerated.

Conclusion

The objectives of auditees and improved audit outcomes will not be achieved if poor internal controls and instability are not addressed (**DO**) and the leadership and officials are not held accountable through implementing consequences for transgressions, a lack of action and poor performance (**ACT**)

.

NOTES

15 Recommendations

15. Recommendations

All role players in national and provincial government should continue to work together to strengthen the capacity, processes and controls of departments and public entities, which will enable credible financial and performance reporting, compliance with key legislation, sound financial management and improved service delivery. The recommendations that follow are consistent with our messages over the past years and are grouped according to the drivers of internal control, as well as linked to the plan+do+check+act cycle.

Leadership

1. In order to improve and sustain audit outcomes, auditees require effective leadership (political and administrative) that is based on a culture of honesty, ethical business practices and good governance, protecting and enhancing the interests of the auditee.

   The following are some of the key aspects that should be considered:

   - Implement the required formal codes of conduct and regularly communicate their existence and continued applicability to officials.
   - Monitor key officials' performance regarding the maintenance of adequate systems of internal control that ensure credible monthly financial reporting, reliable reporting against predetermined objectives, and compliance with key legislation.
   - Establish clear lines of accountability.
   - Take corrective or disciplinary action against key officials for misconduct.
   - Honour commitments for interventions made to us in response to audit outcomes.

2. Policies and procedures should be applied fully to enable auditees to implement **consequence management** for officials who fail to comply with the applicable legislation, while appropriate and timely action must be taken against transgressors. A less tolerant approach should be followed by all parties, including those charged with governance and oversight, which will result in accountability being enforced and consequences being instituted against those who intentionally fail to comply with legislation.
3. Executive authorities and accounting officers or authorities should ensure **stability in key senior management positions**, specifically those of accounting officers, chief financial officers and heads of SCM units. The ability to attract and retain competent officials remains a major challenge, but is key to consistent performance and a strong control environment.
4. Accounting officers and authorities should insist on **credible in-year reporting** on financial and service delivery performance and in particular on the progress and achievement of targets of key projects.
5. Government should work towards a **consistent strategy** for SOEs, which includes firm commitments to support viable SOEs where the economic climate is affecting their sustainability. The **oversight** by the departments, ministers and parliamentary committees responsible for the SOEs should include strong in-year monitoring and ensuring that governance policies and practices are in place. Boards and chief executive officers should be **held accountable** for the deliverables and financial results of the SOEs, and there must be immediate and effective consequences for poor performance and transgressions.

Financial and performance management

1. **Proper and timely record keeping** ensures that complete, relevant and accurate information is accessible and available to support financial and performance reporting. Sound record keeping will also enable senior management to hold staff accountable for their actions. A lack of documentation affects all areas of the audit outcomes, including SCM. Senior managers should therefore ensure proper record keeping so that records supporting financial and performance information as well as compliance with key legislation can be made available when required for audit purposes. They should also implement policies, procedures and monitoring mechanisms to manage records and make staff members aware of their responsibilities in this regard.
2. Controls should be in place to ensure that **transactions** are processed in an accurate, complete and timely manner, which in turn will reduce errors and omissions in financial and performance reports.

   Some of the matters requiring attention from senior management include the following:

   - Daily capturing of financial transactions, supervisory reviews of captured information, and independent monthly reconciliations of key accounts.
   - Collecting performance information at intervals appropriate for monitoring, setting service delivery targets and milestones, and validating recorded information.
   - Confirming that legislative requirements and policies have been complied with before initiating transactions.
3. Accounting officers should ensure that auditees have mechanisms to **identify applicable legislation** as well as changes to legislation, assess the requirements of legislation, and implement processes to ensure and monitor compliance with legislation. **Compliance checklists** should be implemented as a tool to supplement policies and procedures. These will enable officials, supervisors and monitoring units (e.g. internal audit units) to independently check whether all legislative requirements are met in the daily transactional, management as well as SCM processes.
4. **Regular reports** to management and governance structures on compliance with key legislation, specifically in the area of SCM, will further promote awareness of legislative requirements and ensure that management deals with compliance in a regular and structured manner.
5. The implementation of **audit action plans** and the quarterly monitoring thereof to support financial management and governance at auditees should be prioritised.

   The matters requiring attention by accounting officers and senior managers include the following:

   - Devise action plans to specifically address the external and internal audit findings.
   - Assign clear responsibilities to specific staff members to carry out action plans and ensure that these responsibilities are executed effectively and consistently through monitoring.
   - Develop audit action plans early enough in the financial year to resolve matters by year-end.
   - Ensure that audit action plans address all three areas of audit outcomes, namely qualifications, findings on performance reports and non-compliance with legislation.
   - Focus the actions to be taken on the root causes of findings, thereby ensuring that sustainable solutions are found.

6. Management should specifically focus on improving the **IT control environment**. The following actions should be taken:
   - Chief information officer and IT manager positions should be filled with appropriately qualified and experienced persons, and the shortage of IT skills on lower levels should be addressed.
   - Policies, standards and procedures should be sufficiently documented, implemented and monitored for compliance. Continued efforts should be made towards implementing the IT governance framework and continuous monitoring of the implementation and operating effectiveness of governance structures already established should be prioritised.
   - The weaknesses in security management, user access management and IT continuity should also be addressed before the risks created by these weaknesses materialise.
   - Management should ensure that service providers are monitored on a regular basis and that corrective actions are taken against them where deviations from the expected quality and standards are detected. A plan for the transfer of skills should be required when vendors bid for work at auditees.
   - Reporting on key service delivery at auditees needs to be improved by investing in application systems with built-in key automated controls that can provide additional assurance to the public and those charged with governance.
7. Management should ensure that the arrangements with **implementing agents** are clear in terms of responsibilities and deliverables, including the SCM principles to be followed and the accounting to be done on the projects. The activities and deliverables of implementing agents should also be monitored.
8. The **financial position of departments** will only improve if expenditure is more effectively monitored in-year, when incurred (and not just when paid), and by improving systems to promptly account for liabilities incurred. At both departments and public entities, the process and controls to ensure effective **revenue collection and payment of creditors within 30 days** should receive attention.

9. Reducing the cost of services provided is part of the solution for **improved financial health**. We believe that more could be done with less if, among other cost-saving initiatives, a concerted effort is made to curtail the extent and costs of using external providers. The SCM process should be used effectively to procure goods and services from the best-qualified providers at the best price – and only if the need cannot be addressed internally or through other means.
10. The capacity and capability of departments and public entities **to plan, manage and report on service delivery** need urgent and increased attention. **Project management** is required for key projects to succeed and auditees should be guided and supported in a more focused manner in this regard.
11. Departments responsible for key programmes of government should implement robust financial and performance management systems that will ensure credible monitoring and reporting of financial and non-financial information. Corrective steps should be taken timeously if the monitoring process highlights any project failures and targets not being achieved.

Governance

1. Executive authorities, accounting officers or authorities and senior managers should implement the recommendations of **internal audit units and audit committees** and use the opportunity to interact with these bodies to assist in improving governance and control.
2. The accounting officer or authority supported by the executive authority should focus on the following:
   - Ensure that there is an **adequately resourced and functioning internal audit unit** overseen by the audit committee that can identify internal control deficiencies and recommend corrective action effectively.
   - Ensure that the **audit committee promotes accountability and service delivery** through evaluating and monitoring responses to risks and providing oversight of the effectiveness of the internal control environment, including financial and performance reporting and compliance with legislation.
   - 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.
3. Areas where these governance structures can jointly **make significant contributions** to the audit outcomes include the following:
   - Encourage senior management to submit regular financial and performance reports for audit committee review.
   - Assist with designing the audit action plan and monitor the implementation thereof.
   - Review financial statements and performance reports before submission for auditing to identify material misstatements.
   - Monitor the appropriateness and timeliness of actions taken by management in instances of known transgressions by officials.
   - Escalate matters of concern raised by the audit committee to the executive authority to be dealt with as appropriate.
   - Track and prioritise items that could derail the audit outcomes.
   - Play a more active and effective role in tracking the progress made in implementing management commitments in respect of previously raised IT audit findings and in improving IT controls generally.
4. The audit committee chair needs to play a leading role in ensuring that the committee remains focused on ensuring that **management fulfils its responsibilities**.
5. Departments that **oversee public entities** should ensure that they receive credible in-year reporting on the financial health of the public entities and timeously intervene or provide support where problems are identified.

Conclusion

In order for national and provincial government to position itself to achieve the goals as set out in the MTSF, it is vital that the leadership and management diligently execute their responsibilities to enable a professionalised national and provincial government that embraces the concepts of transparency and accountability. The enabling role of the accounting officer and the oversight functions of executive authorities will play an important role in creating an environment where effective, efficient and economical service delivery and a clean audit are natural products of performing the correct actions. By implementing these simple practical steps, substantially improved financial management and performance reporting can be brought about. This is a goal within reach and a key ingredient in building trust in the credibility and accountability of national and provincial government and its capacity to deliver services to citizens. All auditees should keep striving to improve accountability, good governance and consequence management to attain or maintain clean administration.

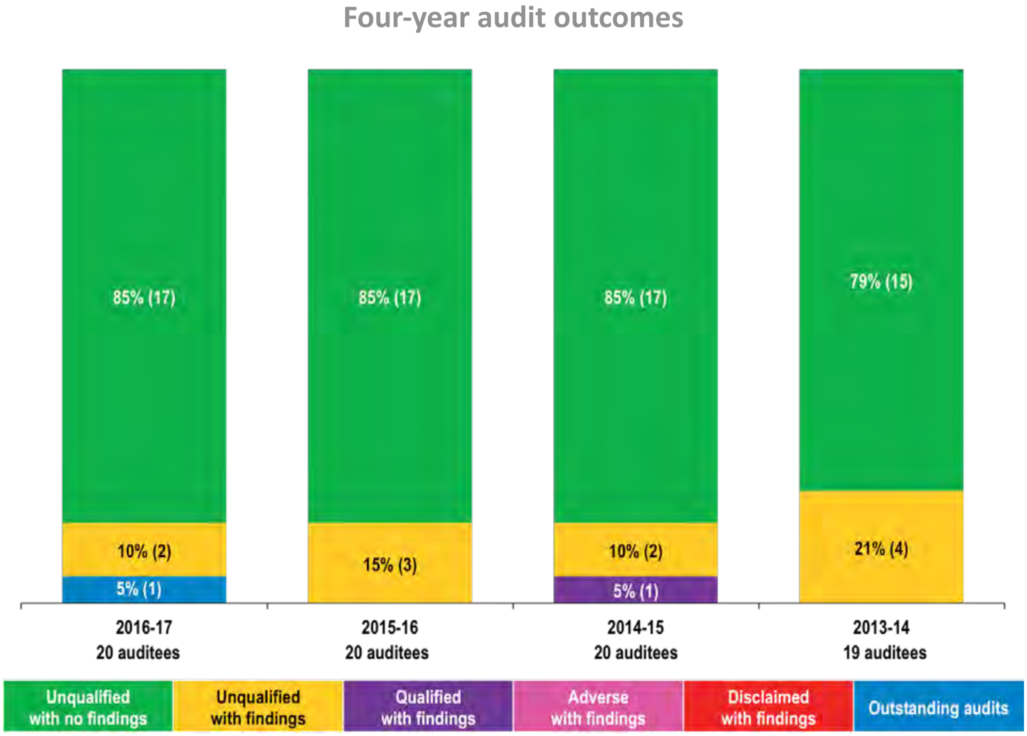
In conclusion, we again draw your attention to the plan+do+check+act cycle that can be used when implementing our recommendations.

Figure 1: Plan+do+check+act cycle – committing to accountability

16 Provincial overviews

The Western Cape and Gauteng continued to produce the best results – with 85% and 52% clean audits, respectively. The improvement made year-on-year was mostly sustainable. Common in both provinces was the role of the leadership in instilling a culture of accountability and expecting nothing less than sound administration. Members of the executive councils and provincial treasuries have a common goal of clean administration and, under the leadership of the premiers, are working systematically towards that goal in spite of facing similar challenges as the other provinces.

16.1 Western Cape



The Western Cape provincial government consists of 24 auditees, including 14 departments and 10 entities. As part of our audit methodology, we classified four entities as small auditees based on their importance and the size and nature of their business. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, it would have reflected an improved picture for 2016-17, with 21 auditees (88%) receiving clean audit outcomes, two auditees (8%) obtaining financially unqualified opinions with findings, and one auditee whose audit was outstanding (4%).

The overall provincial audit outcomes of the Western Cape remained unchanged compared to the previous year, with a slight improvement in audit outcomes over the past four years as a result of the leadership in the province continuously leading by example. The leadership insisted on a culture of accountability and sound management practices, while the political leadership continued to focus on clean administration. Two departments were financially unqualified with findings, namely Human Settlements that regressed from financially unqualified with no findings and Health that remained unchanged. Both departments had material findings on the reliability of their performance reports. The other 10 provincial departments, the provincial parliament and four entities were able to sustain their financially unqualified audit outcomes with no findings from 2015-16. The Western Cape Housing Development Fund and the Western Cape Nature Conservation Board improved from unqualified opinions with findings in the previous year to unqualified opinions with no findings this year. The audit outcome of Agriculture is outstanding pending the finalisation of a technical matter related to an interpretation of whether the agreements in place with Casidra and one other private entity should be accounted as transfer payments or goods and services.

It is encouraging that we did not report material compliance findings at any auditee. This is an improvement from the previous year when one auditee had a material compliance finding relating to corrections in the financial statements.

Irregular expenditure increased slightly from R18 million in the previous year to R23 million in the year under review. The increase was mainly due to procurement without competitive bidding or quotation processes as well as non-compliance with legislation on contract management and other procurement process requirements. Although we reported no material non-compliance with legislation during 2016-17, mainly due to most managers taking accountability through regularly monitoring and reviewing compliance with legislation, we are still concerned about the immaterial findings on SCM. If these are not addressed, they have the potential to lead to a regression in the audit outcomes. Four auditees had immaterial compliance findings related to local content requirements not having been followed – this was the area within SCM that had findings at the highest number of auditees.

Overall, five auditees submitted performance reports that contained material errors, as was the case in the previous year. The main reasons for material misstatements were the inadequate review of performance information and inadequate processes to prepare accurate and complete information for reporting purposes. The quality of performance reports remains a concern for the sustainability of clean audit outcomes, as Human Settlements and Health were unable to correct their performance reports, resulting in these departments obtaining unqualified opinions with findings.

The analysis of financial viability shows an overall improvement in the status of financial health of departments. Of concern, however, are three departments with more than two unfavourable indicators. The indicators for these departments included an accrual-adjusted net current liability position at year-end (which meant that current liabilities exceeded current assets), an accrual-adjusted deficit at one department (where expenditure exceeded total revenue), and a debt-collection period after impairment exceeding 90 days at two departments. It is important that departments appropriately manage the amount of accruals and payables to limit the impact on their working capital.

The leadership insisted on a culture of accountability and sound management practices, while the political leadership continued to focus on clean administration in the province.

We audited the key programmes included in the ENE and selected key projects that support these programmes – we tested 16 projects at six departments. Our procedures included determining whether grant money had been spent for the intended purpose, whether procurement processes had been followed, whether programmes funded by grants had been evaluated, and whether planned targets or milestones had been achieved. Generally, departments applied good planning and project management principles, monitored spending against the budget, and followed the required procurement processes.

There was a slight improvement in the number of vacancies in key positions. All chief financial officer and senior management (for monitoring and evaluation) positions were filled at the end of 2016-17; while one position that became vacant during 2015-16 in each of these categories was subsequently filled. Stability in these key positions is important to sustain and improve audit outcomes and the control environments of financial and performance management and compliance with legislation.

The drivers of key controls indicated that the leadership-related controls were sustained for the past three years, mainly due to the stability and accountability in leadership roles and established policies, procedures and processes. Financial and performance management key controls were not sustainably effective at four auditees, considering the adjustments to performance reports and other immaterial findings reported. With regard to governance, audit committees and internal audit units were in place at all auditees and were robust and proactive regarding the implementation and monitoring of action plans to address internal control deficiencies. This contributed to the sustained audit outcomes.

We assessed IT controls in the areas of IT governance, security management, user access management and IT service continuity management. We also considered the work of internal audit units in terms of the nature, scope and timing of the work performed. The internal audit units' work on the IT service continuity focus area was used and findings per department were reported as part of the external audit. The work and findings of the IT application security review performed by the internal audit unit at one of the entities were also used.

Although auditees made progress in addressing prior year IT audit findings, departments experienced challenges with the implementation of controls in the areas of IT service continuity and user access management. Nine departments regressed in the area of IT service continuity due to the inadequate testing of disaster recovery plans. The user access management focus area showed a net regression of one department as a result of the inadequate implementation of controls for reviewing system administrator activities and failed login attempts. An analysis of the overall IT audit outcomes for departments indicates a regression from the previous year due to the regressions in these focus areas. Entities made significant progress in addressing prior year findings through the implementation of corrective measures. This was evidenced by four of the entities having no significant findings. There was also a reduction in the number of findings at the other entity.

The slow management response to risks identified and to improve internal controls supporting the reliability of reporting on all indicators was the root cause of the only material findings that remained in the province. We reported immaterial findings in 2015-16 at Health and Human Settlements on some of the same indicators, which escalated to the audit report in 2016-17.

Our assessment of assurance providers confirmed that the required level of assurance provided by most of the key role players contributed to the overall audit outcomes in the province. Senior management should, however, strengthen and speed up the implementation of controls in performance reporting. The executive leadership continued with commitments made in the previous year relating to their monitoring and implementation of the corporate governance and review outlook process.

The provincial treasury also continued its support and guidance through budgetary control, monitoring monthly reports, and enforcing financial management practices. It is pleasing to note that these initiatives contributed to the province not incurring unauthorised expenditure for the fifth consecutive year.

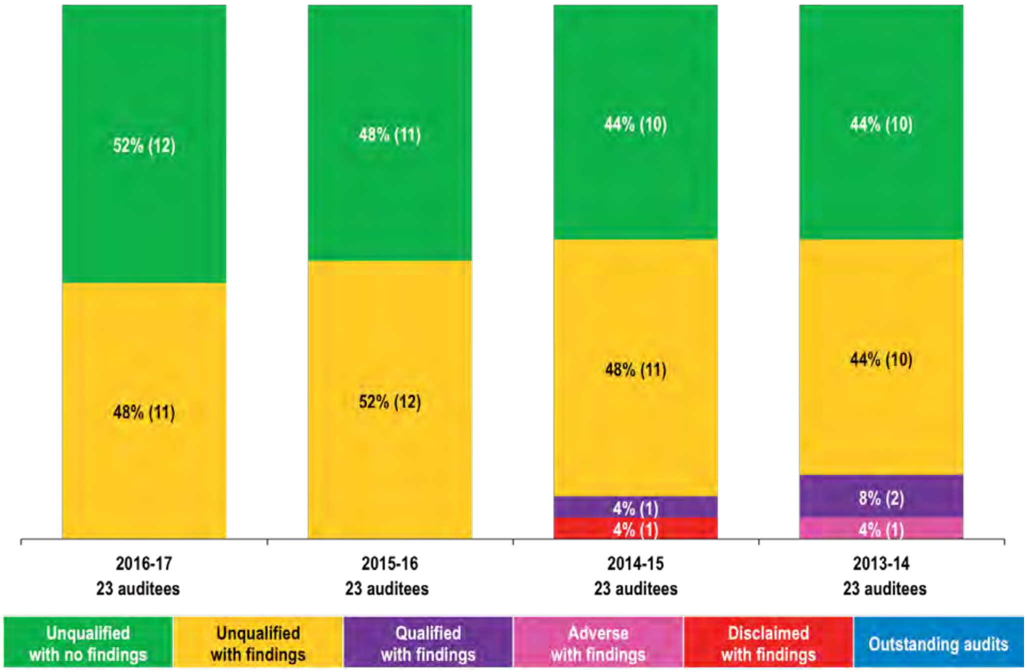
Accounting officers, accounting authorities and senior management are committed to achieving and maintaining clean administration as well as providing consistent oversight to ensure that the required action is taken where weaknesses in controls are reported. Furthermore, consequence management is applied through investigations, as required by legislation, and appropriate action is taken to hold officials accountable, where applicable. The assurance provided by audit committees through their oversight continued to contribute to the drive towards clean administration.

In order to sustain and improve the audit outcomes in the province, the following actions should be taken:

- The administrative and political leadership should continue to take accountability for their commitments and act timeously when implementing effective and sustainable internal controls that support credible financial and performance reports and compliance with key legislation.
- Accounting officers and accounting authorities should hold senior management accountable for processes implemented in relation to performance reports being supported by sufficient and credible evidence for all programmes reported on.
- Accounting officers and accounting authorities should continue with all good practices that are already in place and improve the review of controls in place to facilitate improved compliance with procurement legislation, such as the use of compliance checklists by auditees to avoid a regression in this area.
- Oversight committees should continue to collaborate with each other and improve key oversight activities, including the timely tabling and regular follow-up of key resolutions.
- Accounting officers and accounting authorities as well as senior management should implement basic internal controls and accounting disciplines effectively by preparing regular and accurate financial statements and performance reports, to enable governance structures to sufficiently review them. They should further implement processes to ensure an adequate and timely response to any new accounting, performance reporting and compliance developments to facilitate accurate reporting.

16.2 Gauteng

Four-year audit outcomes



The Gauteng provincial government consists of 34 auditees, including 15 departments and 19 entities. As part of our audit methodology, we classified 11 entities as small auditees based on their importance and the size and nature of their business. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, it would have reflected a much improved picture for 2016-17, with 22 auditees (65%) receiving clean audit outcomes and 12 auditees (35%) obtaining unqualified opinions with findings.

The Gauteng provincial government improved its audit outcomes over the past four years. It is encouraging to see eight auditees (35%) sustaining their clean audit outcomes, by institutionalising internal controls over financial management, performance reporting and compliance with legislation. It is commendable that no auditee regressed in the current year, with one auditee, namely Gauteng Enterprise Propeller, joining those with a clean audit outcome in 2016-17.

The premier, speaker and members of the executive council continued to lead by example and thereby strengthened accountability. The premier, with the support of the members of the executive council, insisted on a culture of accountability and sound financial management practices and demonstrated timely and effective consequence management where non-performance was identified, as we have seen senior officials found guilty of financial misconduct being dismissed, including accounting officers. The political leadership continued to focus on the premier's vision of a clean administration (termed 'going green') by working effectively with the administrative leadership and holding them accountable for the implementation of sound internal controls and financial management practices. Coordinating departments and external oversight structures sustained their oversight responsibilities to further improve governance within the province.

Health and g-Fleet Management, with the continued assistance of consultants, managed to sustain their unqualified audit opinions; however, the sustainability of the current audit outcomes remains at risk as they still have not addressed the recommendation to implement a clear business continuity plan for the transfer of knowledge from the consultants and to institutionalise internal controls. The accounting officer at Health was slow to respond to the urgent need to upgrade the health recording system to provide accurate and reliable information for financial reporting. Although all auditees submitted their financial statements for auditing on time, material misstatements were identified at eight auditees (35%), which were corrected during the audit. This was because chief financial officers failed to implement basic financial disciplines and regular financial reporting controls during the year, which is not a sustainable practice.

Despite a slight improvement in the number of auditees that complied with key legislation, all 11 auditees (48%) that failed to achieve clean audit outcomes, as in the previous year, had material findings on compliance with key legislation. This remains the major factor preventing the province from improving its audit outcomes. The administrative leadership and senior management's response to commitments to address compliance findings, specifically those relating to expenditure management and SCM, was slower than expected.

As a result, the irregular expenditure remained high at R5,9 billion (2015-16: R6,5 billion). Most of the irregular expenditure incurred related to payments made against non-compliant contracts awarded in previous financial years at Roads and Transport (bus subsidy legacy contracts to the value of R2,3 billion), and without following the proper procurement and contract management process at Health and Human Settlements. Notwithstanding the high value of irregular expenditure, we determined that goods and services were received for most of the irregular expenditure relating to non-compliance with SCM requirements. Accounting officers should ensure that rigorous investigations are conducted and that steps are taken to recover losses, if identified. The premier and the member of the executive council responsible for finance honoured their commitment to fast-track the implementation of the open tender process. The shortcomings identified during the early implementation stages of this process must be addressed to ensure the intended positive impact thereof across all departments in the province and to reduce irregular expenditure.

The quality of performance information regressed and remains a concern. Although only five auditees (23%) had material findings on their performance information, another eight auditees (36%) relied on the audit process to correct the reliability of the information in the final performance report. With the provincial focus on service delivery through the transformation, modernisation and re-industrialisation plan, it is critical that actual performance is reported accurately. Accounting officers and accounting authorities should hold heads of monitoring and evaluation units accountable for ensuring that sound processes are in place to confirm that performance information is supported by sufficient and credible evidence. In addition, the provincial IT strategy must provide solutions where information systems are not stable and secure to produce accurate and verifiable information.

IT remains critical in ensuring the confidentiality, integrity and availability of information to enable accurate reporting, service delivery and national security as well as to promote effective oversight. The provincial IT environment showed little progress since the previous year due to the slow response from accounting officers to improve the stability of chief information officer positions and hold senior management accountable for implementing action plans. Despite the stagnation, best practices were observed at some auditees, including the accounting officers prioritising and taking ownership of IT matters through effective monitoring mechanisms. Accounting officers and accounting authorities must ensure that the IT units are fully staffed with skilled resources and that IT governance processes are adequately monitored to improve the areas of user access management, security management and IT service continuity controls.

The status of financial health remained unchanged, with no auditees experiencing significant going concern challenges. Education, Health and Human Settlements, which constitute about 79% of the provincial budget, would have incurred unauthorised expenditure had all their accrued expenses been paid by year-end, which placed additional pressure on the service delivery objectives of the following financial year. The provincial leadership should safeguard against the increased risk of lawsuits and claims at Health, which would place further strain on the department's financial resources.

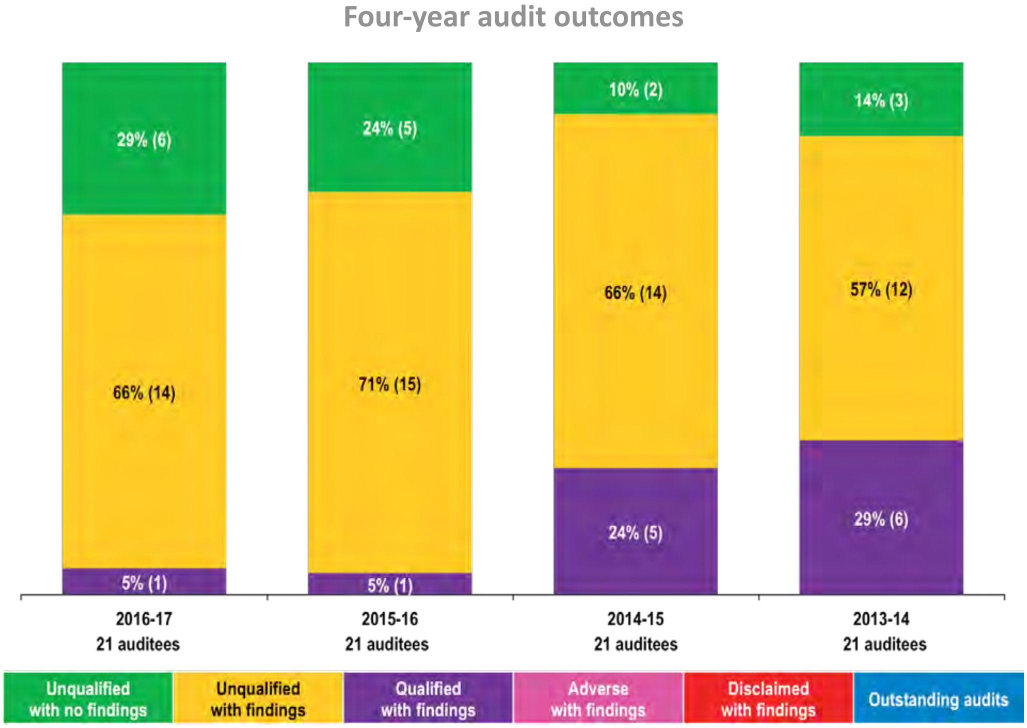
The province used 99% of the R18,8 billion in conditional grants made available to departments in 2016-17 to deliver services to the citizens and in most cases accounted correctly for these in the financial statements. However, at Human Settlements, the human settlements development grant was not spent in accordance with the applicable grant framework, which resulted in irregular expenditure, and key project milestones were not achieved. The accounting officer must hold senior management accountable to improve planning and the spending of government funds.

The Gauteng provincial government has improved its audit outcomes over the past four years. In order to sustain and further improve the audit outcomes, the premier, speaker and members of the executive council must continue to lead the way and positively influence a culture of accountability, improving financial governance and reducing irregular expenditure.

The premier committed to continue oversight and acceleration of provincial initiatives for the achievement of clean administration across the province, aiming for 75% of all auditees attaining clean audit outcomes in 2017-18. The accounting officers and senior management should perform their duties with the required discipline and respond proactively by improving internal controls and paying greater attention to filling vacancies in key positions. Audit committees and internal audit units need to improve their oversight to ensure that controls over financial management, compliance with legislation and performance reporting improve and are embedded. Portfolio committees need to intensify their focus on holding auditees accountable for accurate and complete performance information, while the public accounts committee's accountability mechanism should be improved and formalised. We will continuously track the commitments made and actions taken by the political and administrative leadership to determine whether they yield the desired impact of improving financial governance, reducing irregular expenditure and further improving the overall audit outcomes of the province.

The audit outcomes of the **Eastern Cape and Limpopo improved** over the past four years. In the Eastern Cape, the provincial treasury played a significant role in these improvements through not only responding to our recommendations but also actively seeking our advice. The province is, however, plagued with poor SCM practices and project and service delivery failures for which there is little accountability and consequences. In Limpopo, the improvements can be attributed to the political leadership taking accountability and discharging oversight responsibility through robust discussions and interrogation of reports submitted by the administrative leadership. However, poor asset management systems and record keeping contributed to a qualification on capital movable assets at six departments.

16.3 Eastern Cape



The Eastern Cape provincial government consists of 25 auditees, including 14 departments and 11 entities. As part of our audit methodology, we classified four entities as small auditees based on their importance and the size and nature of their business. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, it would have reflected an improved picture for 2016-17, with 10 auditees (40%) receiving clean audit outcomes. The leadership of the Eastern Cape Liquor Board is congratulated on achieving this outcome during the year under review, while the leadership of the remaining three small auditees is congratulated on maintaining this outcome.

The provincial audit outcomes improved by 39% over the past four years. The most significant improvement occurred during 2015-16. We are encouraged by the improved accountability and good governance displayed by Rural Development and Agrarian Reform, which contributed to it improving to an unqualified audit opinion with no findings from an unqualified opinion with findings in the previous year. We further recognise the political and administrative leadership of the provincial treasury, Safety and Liaison, Eastern Cape Parks and Tourism Agency, Eastern Cape Rural Development Agency and East London Industrial Development Zone for maintaining their clean audits. The leadership of the provincial treasury is also recognised for the significant role it played in the province's improved and sustained outcomes by proactively engaging our office on transversal audit issues, technical issues and specific auditee matters.

The control environments of those departments and entities that did not achieve clean audits remained a concern. The slow response by accounting officers and senior managers to implement our recommendations relating to enforcing a culture of basic daily, weekly and monthly financial management disciplines and adhering to good controls contributed to these poor control environments. Controls in the IT environment remained concerning and improved only slightly from the previous year.

In response to the 2015-16 outcomes, the provincial leadership committed to filling critical vacant posts at Education, including the position of head of department; ensuring better communication and coordination between district offices and the head office, thereby enabling effective service delivery at schools; and maintaining appropriate records for credible financial and performance reporting. We commend the premier's office for assisting Education with the commitment relating to the filling of the head of department post and exercising its oversight role by intervening in the challenges faced by the department related to the delivery of school infrastructure.

Although some of these commitments were honoured, Education, which represents 44% of the provincial budget, retained its qualified opinion. This was despite the use of management and financial consultants that were paid R253 million during the year under review. The number of qualification areas increased to five from three in the previous year. Instability in leadership, including acting personnel at head of department (for eight months during the year before the permanent appointment), chief financial officer and senior management levels, resulted in a lack of accountability and good governance and a weak control environment at this department. In addition, an appreciation of the role of applying consequences for transgressions and poor performance was not evident in restoring the integrity of, and building public confidence in, the department's management practices.

The quality of the submitted financial statements improved over the last four years, with only 38% requiring material adjustments. Material amendments were required to the financial statements of Roads and Public Works despite it using consultants at a cost of R39 million to manage its finance function and prepare its financial statements.

The quality of the submitted performance reports stagnated over the last four years, with 62% requiring material adjustments. The usefulness of the reported performance regressed slightly from 19% (four) of the auditees with findings during the previous year to 29% (six) with findings during the year under review. The reliability of the reported performance remained at similar levels than in the previous year (33% or seven auditees with findings). The departments with findings in this area did not ensure that there were adequate systems and processes to collect, collate and record information on actual performance.

> There has been a slight improvement in the Eastern Cape's audit outcomes. However, the province is still struggling to prevent irregular expenditure and enforce consequences for SCM transgressions.

In our previous general reports, we expressed concern over the culture of procuring goods and services without complying with legislation and the lack of consequences for the legislative transgressions, which resulted in cumulative irregular expenditure of R4,9 billion at the end of the previous year. The provincial leadership responded by committing to investigate the irregular expenditure disclosed, holding those responsible accountable, applying a zero-tolerance approach to breaches of procurement processes, and preventing irregular expenditure going forward. Although it is encouraging that 82% of the auditees that contributed to this irregular expenditure demonstrated accountability by investigating the irregular expenditure disclosed by them, only R3,5 million was recovered from the responsible officials. Despite the above commitments, the province incurred irregular expenditure of R2,4 billion in the year under review alone, which was almost double the previous year's amount. Education contributed R1,9 billion to the amount disclosed, while Roads and Public Works contributed R303 million. The level of accountability at Education requires intervention, as the department's contribution to irregular expenditure included an adjustment of R1,1 billion to correct the previous period's under-disclosures. The amount of irregular expenditure incurred by the province could be substantially higher, as Education further disclosed that it was still investigating potential irregular expenditure of R1,1 billion and was also qualified on the completeness of the amount of irregular expenditure disclosed.

The accounting officers used their discretion to appoint targeted suppliers without ensuring that the requirements of the PFMA and SCM Regulations were correctly applied. One such example related to the awarding of a printing tender to the value of R125 million where the bid specifications were restricted through the inclusion of criteria relating to the turnover and the location of the supplier. These criteria effectively excluded all other printing companies that may have wanted to tender. This is contrary to the principles of a fair, equitable and transparent procurement and provisioning system, as required by section 38(a)(iii) of the PFMA. Another department constructed a juvenile detention centre for R49 million to house 60 children in Burgersdorp without first conducting a feasibility study. After construction, the department awarded a contract to the value of R128 million for the management of the facility over a period of five years. The accounting officer used his discretion to award the management contract despite his bid adjudication committee and the provincial bid adjudication committee not recommending the appointment because the process followed had not been fair, equitable or transparent, as required by section 38(a)(iii) of the PFMA.

We applaud the accounting officers for developing effective planning systems, which set defined targets that were aligned to the government priorities outlined in the MTSF. The only exception related to the procurement from local businesses and small, medium and micro-sized enterprises and the payment of these within 30 days, which are central to the provincial economic growth strategy and the priorities of the provincial leadership. We further applaud the accounting officers for ensuring that spending was aligned to overall government priorities. The spending patterns of departments and public entities were predictable, consistent and according to cash-flow management principles. The notable exception was Education, where 39% of the budget was spent in the last month of the financial year and 13% on the last day of March, posing a risk of fiscal dumping. In addition, Education spent 99% of its budget but only achieved 20% of its targets. This poses a risk to the achievement of the department's service delivery objectives, which include improving the lives of people through the provision of quality education.

Infrastructure delivery is a key priority contained in the MTSF. We identified weak control environments and a lack of proper systems and processes around project execution and commissioning and the use of infrastructure as the areas that require the most leadership attention in this regard. The main findings in these areas included inadequate supervision and monitoring of contractors, poor quality management, and projects not completed within budget or within the planned time resulting in delayed commissioning and use of projects. For example, additional costs of R19 million were incurred on a clinic, which had an original budget of R28 million, because the contractor had to be replaced and quality issues were not addressed timeously by the project managers. An example of delayed commissioning and use related to upgrades to an existing hospital, which was not used because the hospital in question did not have a facilities manager to manage the use of the new facilities.

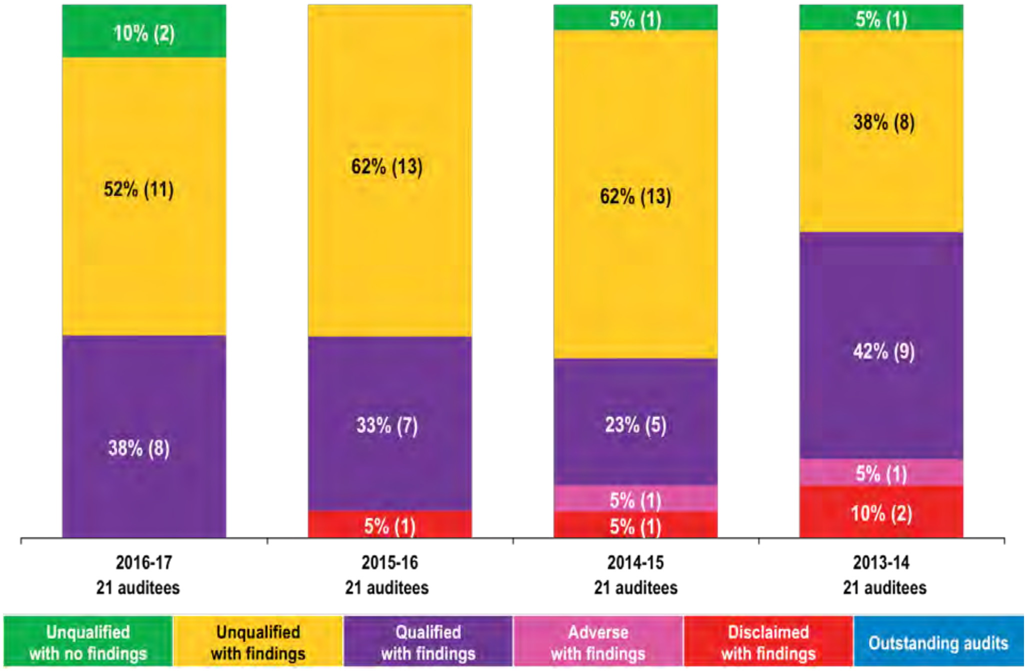
In order for the province to grow the economy to the target of 5% per year as set out in the MTSF and to provide the social services as promised, its strategic departments and public entities have to be financially viable. Five departments (Education, Health, Roads and Public Works, Social Development, and Human Settlements) that together constitute 87% of the provincial budget, one strategic economic driver entity (Coega Development Corporation) and the Mayibuye Transport Corporation may require additional funding to maintain their existing levels of services. Human Settlements disclosed commitments to build houses, payables and accruals to the value of R13,1 billion, while Health disclosed R16,9 billion in contingent liabilities relating to medical claims, which were not budgeted for, and commitments and accruals of R2,6 billion. We are particularly concerned about the impact of these amounts on future budgets and on the finances of the province as a whole. A shortage of skilled medical practitioners, poor access to emergency medical services, poor record keeping relating to patient files, faulty equipment and a shortage of necessary equipment were identified as contributing factors to the increased medical claims against Health.

To further improve the audit outcomes in 2017-18, the provincial leadership committed to providing support to Education by assisting the department to address its qualification areas, monitoring its spending and dealing with medical legal claims as well as pushing at least 50% of the departments to achieve unqualified opinions with no findings. The provincial leadership also re-committed to reducing irregular expenditure caused by SCM non-compliance and monitoring the implementation of consequence management.

All assurance providers should improve their monitoring and oversight to ensure that internal controls are effective and further improvements in audit outcomes are achieved. In particular, the provincial leadership should set a leadership tone that promotes accountability, ethical behaviour and transparency. The lack of accountability and the failure to adhere to financial management disciplines at Education should be dealt with swiftly to salvage this department.

16.4 Limpopo

Four-year audit outcomes



The Limpopo provincial government consists of 23 auditees, including 13 departments and 10 entities. As part of our audit methodology, we classified two entities as small auditees based on their importance and the size and nature of their business. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, it would have reflected a much improved picture for 2016-17, with three auditees (13%) receiving clean audit outcomes and 12 (52%) obtaining unqualified opinions with findings.

The province had improved its audit outcomes from the previous year, with two clean audit opinions achieved by the provincial treasury and the Limpopo Gambling Board, three public entities improving to unqualified audit opinions with findings from prior year qualifications, namely Roads Agency Limpopo, Gateway Airports Authority Limited and Limpopo Tourism Agency, and Education improving to a qualified audit opinion from being disclaimed for five consecutive years. The audit outcomes of two departments and one public entity regressed to a qualified opinion, namely those of Agriculture and Rural Development; Cooperative Governance, Human Settlement and Traditional Affairs; and the Limpopo Economic Development Agency. The regression at the latter is of concern, as the entity plays a significant role in driving the special economic zone and rolling out the infrastructure broadband telecommunication programme in Limpopo, which is expected to create jobs and boost economic activity.

Improvements can be attributed to the political leadership taking accountability and discharging oversight responsibility through robust discussions and interrogation of reports submitted by the administrative leadership. The premier honoured his commitment from the prior year to improve audit outcomes and to hold the executive leadership accountable for the outcomes. The executive leadership updated the premier on the status of the expected audit outcomes during a special meeting in mid-June. The provincial treasury also played a key role in the improved outcomes by intensifying its engagements at chief financial officers' forums, and further accepted our proposal to have bilateral meetings to discuss the audit process, related technical and legal matters and any other concerns from both parties. These engagements were very positive and ensured that each party carried its own accountability baton.

During 2011-12, the province was placed under section 100(1)(b) administration in terms of the country's constitution. Following the withdrawal of the administration team in 2015, the provincial treasury placed Education under administration in terms of section 18(2)(g) of the PFMA for a period of two years. This initiative finally yielded positive results, as the department improved its audit outcome after five consecutive years of obtaining disclaimed opinions. The department appointed the official from the provincial treasury responsible for heading the section 18(2)(g) administration team as the head of department in 2016-17. Her appointment resulted in the right tone being set at the top; and through collaborative efforts with staff, the department was able to improve. This proves the premier's assertion that the appointment of the right people in the right positions will result in improved audit outcomes.

The province implemented the asset management system (BAUD) at all departments in 2016-17, as recommended by the section 100(1)(b) administration team in 2012-13, with the exception of Health. However, poor migration processes and project management during the implementation of the system contributed to a qualification on capital movable assets at six departments. The use of Excel at Health contributed to the stagnant position on asset management. The in-year monitoring and review of asset registers need to be strengthened at these departments.

The overall outcome of the audit of performance reports regressed when compared to the previous year, with 11 auditees having findings in this regard. Four auditees regressed, namely Agriculture and Rural Development; Cooperative Governance, Human Settlement and Traditional Affairs; Corridor Mining Resources; and the Roads Agency Limpopo, at which we raised material findings on the performance reports submitted for auditing. The lack of standardised operating procedures and poor record-keeping practices contributed to findings on reliability, as the auditees were unable to produce supporting evidence to substantiate the reported performance. We reported material findings on the reliability of the reported performance at Health; Education; Public Works, Roads and Infrastructure; and Agriculture and Rural Development on indicators related to conditional grants. We reported SCM compliance findings at Health (revitalisation grant), Education (infrastructure grant), Agriculture (Ilima/Letsema projects grant), and Cooperative Governance, Human Settlement and Traditional Affairs (human settlements development grant). These grants are aimed at addressing social challenges faced by the unemployed and poor communities. The inability of the departments to fairly report on the performance of funds granted to meet key service delivery targets limits the ability of both the provincial and national administration to fairly assess progress and to implement remedial action to address any shortcomings identified.

The political and administrative leadership needs to take decisive steps to enforce zero tolerance for deviations from SCM processes, and consequence management should be implemented to deter the disregard of regulations. An action plan to deal with the repeat instances of non-compliance with SCM Regulations must be developed to ensure that the process for procurement is fair, equitable, transparent, competitive and cost-effective and that value for money is realised for the goods and services procured. The irregular expenditure more than doubled from the previous year to R2,6 billion (2015-16: R1 billion). Two auditees incurred R2,087 billion (81%) of the irregular expenditure, namely the Roads Agency Limpopo (R1,195 billion) and Education (R892 million). The most common compliance findings related to an uncompetitive or unfair procurement process, including not inviting competitive bids, bids not being advertised for the required period, and bid documentation not stipulating the minimum threshold for local production and content. At the Roads Agency Limpopo, R1,060 billion of the R1,195 billion related to non-compliance with SCM Regulations in the previous year, with the entity identifying and quantifying the full extent of the non-compliance and adequately disclosing this amount in the year under review. In addition, two auditees (Agriculture and Education) were qualified on the completeness of the amounts disclosed as irregular expenditure and a further 13 auditees were still investigating the irregular expenditure disclosed to determine the extent of the expenditure incurred. As a result, the total irregular expenditure incurred by the province is understated by an unknown amount. Only R1,6 billion of the R6,5 billion accumulated irregular expenditure at the end of the 2015-16 financial year had been investigated and was condoned (R1,1 billion), identified as recoverable from the liable persons (R648 000) or written off as irrecoverable (R511 million) in the current reporting period.

Fruitless and wasteful expenditure increased to R139 million (2015-16: R44 million), R109 million (78%) of which related to an overpayment on the acquisition of land by Cooperative Governance, Human Settlement and Traditional Affairs. The member of the executive council responsible for this department requested that a forensic investigation be conducted into this matter. The province is applauded for not incurring unauthorised expenditure, compared to R555 000 in the previous year. This proves the maturity of financial planning and monitoring processes at auditees.

The financial health of the province improved when compared to 2015-16. Six provincial departments improved while three public entities regressed, with Corridor Mining Resource having a significant financial sustainability challenge. Only Health's bank account was in overdraft compared to three auditees in the previous year, and more than 10% of debts were irrecoverable at eight auditees (2015-16: 10). The province should continue working on strategies to improve debt collection and strengthen the cash-flow position of the province.

Auditees showed improvement over the previous audit cycle on all IT focus areas, with the exception of user account management. The regression in this regard was due to the provincial treasury not updating user account management procedures to include the BAUD system. Improvements at departments were due to the involvement of internal audit units in monitoring findings raised by our office in the previous year. While some departments appointed skilled personnel such as government IT officers, critical IT vacancies had still not been filled at especially Health, Education and Transport. Heads of departments, the premier's office and provincial government IT officers are now involved in monitoring the IT issues reported to ensure that they are resolved. They also provide assistance with the implementation of controls at departments.

The key control environment and the overall level of assurance provided by key role players had also improved, as evidenced by the improvement in the audit outcomes and the achievement of two clean audits. We noted an increased interest by members of the executive council and heads of departments in the auditing process with robust engagements between these stakeholders and audit teams. In the 2015-16 general report, we reported that there were six vacancies at head of department level. These vacancies were significantly reduced with only Sport, Arts and Culture and the provincial legislature not having a permanent head of department at year-end – a head of department was subsequently appointed at Sport, Arts and Culture.

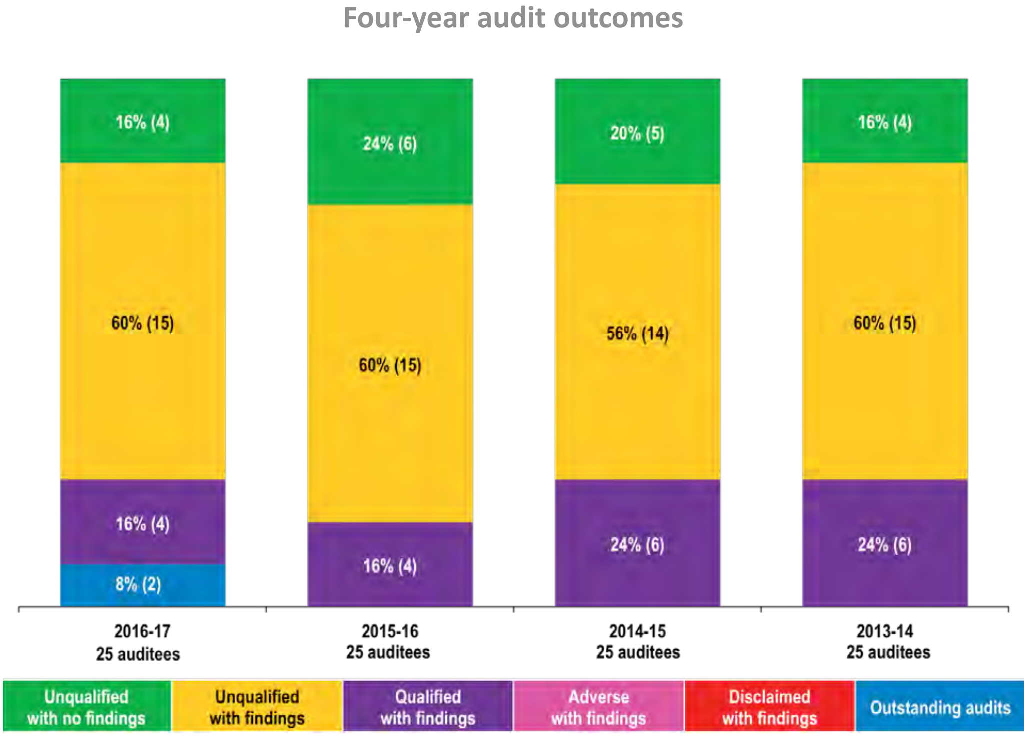
The level of commitment demonstrated by the political and administrative leadership in improving audit outcomes is commendable. The governance structures should intensify their oversight process by robustly interrogating reports submitted to them by departments and public entities to achieve clean administration.

We commend the public accounts committee for clearing the hearing backlog on the 2013-14 and 2014-15 audit outcomes. At the time of writing this report, the 2015-16 hearings for all auditees, except for Cooperative Governance, Human Settlement and Traditional Affairs, Limpopo Tourism Agency and Roads Agency Limpopo, had been concluded and the resolutions tabled. The response by the public accounts committee when dealing with all outstanding hearings following our recommendation last year is encouraging and demonstrates the continued drive towards a culture of accountability, ethical conduct and sound financial management. We once again wish to emphasise that the public accounts committee and portfolio committees should increase their oversight role, as this will ensure that the root causes of poor audit outcomes are collectively dealt with, while improving service delivery outcomes. Our office should furthermore be invited to all portfolio committee meetings to provide insight on matters reported on performance information.

To further improve the audit outcomes and maintain the gains achieved, the premier committed, together with the members of the executive council, to appoint the right people with proper qualifications and implement and monitor action plans at all auditees to ensure sustainable improvements. We have developed a new initiative to enhance our regular engagements with accounting officers and authorities, which is aimed at improving key controls by proactively identifying audit risks that may derail the auditee's progress and result in regressed audit outcomes. The effectiveness of this initiative depends on the administrative leadership's active involvement in developing and enhancing key internal controls to address the identified audit risks, thereby creating a robust internal control system.

The **outcomes in KwaZulu-Natal, Mpumalanga and the Northern Cape were erratic** over the past four years – improvements in the one year were offset by regressions in the following. A lack of urgency by the leadership in honouring commitments and implementing action plans and a slow response to applying consequences were some of the root causes of the outcomes.

16.5 KwaZulu-Natal



The KwaZulu-Natal provincial government comprises 14 departments, the provincial legislature and 20 public entities. As part of our audit methodology, we classified 10 entities as small auditees based on their importance, size, nature and extent of activities. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, it would have reflected a regression for 2016-17, with eight auditees (23%) receiving clean audit outcomes, 20 auditees (57%) unqualified opinions with findings, and five auditees (14%) qualified opinions.

The overall audit outcomes also exclude the results of Ithala Development Finance Corporation (holding company) and Ithala Limited (subsidiary), as the audits of these public entities had not been finalised by the cut-off date for inclusion in this overview. Ithala Limited did not meet certain conditions that needed to be fulfilled as part of the banking licence exemption set out by the minister of Finance, which also delayed its holding company's financial statements.

Over the four-year period, little progress had been made towards improving the audit outcomes. The audit outcomes of six auditees (24%) had improved, 15 (60%) had remained the same, and two (8%) had regressed since 2013-14. It is worth noting that the 15 auditees (60%) with stagnant outcomes included 11 auditees (44%) whose audit outcomes were unqualified with findings.

The provincial treasury and Dube Trade Port maintained their clean audit status over the four-year period. The Sharks Board and Sports and Recreation improved from an unqualified audit outcome with findings in 2013-14 to a clean audit outcome in the current year. These auditees improved their systems and processes by focusing on simple tasks that mattered and were characterised by committed political and administrative leadership and senior management teams with knowledge of important reporting processes. In addition, the shared provincial audit committee robustly engaged with accounting officers and chief financial officers at these auditees, which further contributed to the favourable audit outcomes.
Human Settlements also improved from a qualified opinion in 2015-16 to an unqualified opinion with findings in the current year. The department procured the services of a consultant with the assistance of the provincial treasury to inspect contracts and bid documentation of implementing agents used for municipal construction. This enabled the accurate disclosure of irregular expenditure, which had previously been qualified.

Repeat qualifications at Health and Transport, which account for 42% (R46,60 billion) of the total expenditure budget, have persisted since 2013-14. Notable regressions since the previous year include Agriculture and the Nature Conservation Board that regressed to qualified opinions.
These auditees experienced challenges such as poor record management, breakdowns in regular reporting and reconciliations as well as ineffective monitoring and reviews of reported information. It was also evident that the political and administrative leadership at Health and Transport was slow to implement consequence management for errant officials. Agriculture experienced a breakdown in key controls, as staff did not fully understand the requirements of the financial and performance reporting frameworks due to several vacant posts being filled by acting incumbents. Consequently, there were inadequate monitoring controls over the implementation of asset management policies and procedures and a lack of coordination of financial and performance information from regional sites.

The quality of financial statements submitted for auditing remained a challenge, as 11 auditees (48%) had material misstatements. These auditees continued to struggle with weak internal controls over record keeping, monthly processing and reconciling of transactions as well as regular review and supervision. Seven auditees (30%) received financially unqualified audit opinions only because they corrected all the material misstatements identified during the audit process. It is also concerning that material misstatements were identified in the financial statements of some auditees with fully capacitated finance and chief financial officer positions.

Non-compliance with laws and regulations remains a key hindrance to improving outcomes, as 83% of the auditees did not address compliance findings. Apart from material misstatements, SCM transgressions continued to contribute to the high levels of non-compliance. One of the root causes of non-compliance with key legislation was instability and vacancies in key positions such as those of the accounting officer, chief financial officer and head of the SCM unit. Although members of the executive council displayed a positive attitude and previously committed to implementing mechanisms for the filling of key vacancies and support staff posts, limited progress was made on this commitment.

Some progress had been made on the commitments by the premier's office and the provincial treasury to address weaknesses around irregular and unauthorised expenditure. The support provided to departments assisted in reducing unauthorised expenditure from R218 million in 2015-16 to R106 million in 2016-17, through cash blocking and tighter fiscal policies. Irregular expenditure, however, grew significantly over the year by 218% from R3,57 billion in 2015-16 to R11,35 billion. Most of the irregular expenditure (98%) incurred in the current year related to SCM transgressions. Compliance checklists were not aligned to updates in SCM legislation and/or not implemented in some instances, similar to weaknesses in the previous year, and some departments also had vacancies in head of SCM unit positions.

Health, Human Settlements and Transport requested the provincial treasury to assist in quantifying the full extent of the irregular expenditure to address historical qualifications. Human Settlements disclosed irregular expenditure relating to the prior year of R2,33 billion to address its prior year qualification, whereas Health and Transport were still qualified in this regard. Health, Transport, Human Settlements and Education accounted for R10,68 billion (94%) of the irregular expenditure, which arose mainly due to expired contracts, unjustifiable deviations from procurement processes, non-application of the preference point system, and not following competitive bidding processes. Accounting officers had made minimal progress to ensure that effective consequence management was enforced, as there was an increase in the number of auditees where irregular expenditure was not investigated to determine if anyone was liable for this expenditure. Where investigations were conducted, they were not properly performed and effective disciplinary steps were not taken against officials responsible for the irregular expenditure.

Reporting on performance information regressed, as eight auditees (36%) had material findings in 2016-17 compared to six (27%) in the previous year. In addition, the quality of performance reports had not improved from the previous year in spite of previous recommendations provided. Nine auditees (41%) had performance reports with no material findings only because they corrected the material findings identified during the audit. Education, Health and Transport continued to have material findings on their performance reports. This was as a result of poor record management and inadequate controls over reviewing and reconciling performance information.

The key service delivery departments (Education, Health, Transport and Human Settlements) received R95,87 billion of the total provincial budget (87%). Most of the budgets were utilised with no significant underspending.

Education, which received the largest budget in the province, had significant findings relating to early childhood development (grade R), including classrooms being too small to cater for these school children, teachers not being qualified, and inadequate monitoring of the grade R curriculum. It is encouraging that not many quality concerns regarding the construction of schools were identified on site visits, but poor project management by the department resulted in delays in the finalisation of projects. Poor storage and stock management practices, staff shortages, stockouts and stock losses, insufficient temperature and security controls, and inadequate technology were cited as some of the reasons for the poor health services and high medical claims against Health. Poor project management and implementation, staff vacancies and instability at the coalface of service delivery along with poor governance contributed to the findings we reported.

Transport developed and maintained road networks around the province and fulfilled its role in transporting learners to schools. However, we could not verify whether the department attended to some key safety and compliance areas relating to drunken driving operations and the roadworthiness of vehicles as a result of poor record keeping. At Human Settlements, houses were built with no significant quality control concerns and were being transferred to beneficiaries.

There was uncertainty over the unfunded liability to settle backdated izinduna (headmen) stipends of R1,20 billion at Cooperative Governance and Traditional Affairs. Payments had to be made to the izinduna in the current year based on a presidential proclamation issued in Government Gazette No. 38568 of 2015. The provincial executive council resolved that the department would pay half of the cost through budget reprioritisation, with the balance being proportionately funded by all remaining departments commencing from 1 December 2016. An additional amount of R799,38 million has been projected in terms of the Medium-Term Expenditure Framework to be departmentally funded for izinduna stipend payments, which will place added pressure on departments that currently face cash constraints. Health also disclosed an amount of R10,29 billion for possible medical legal claims; should these materialise, further service delivery setbacks could be expected.

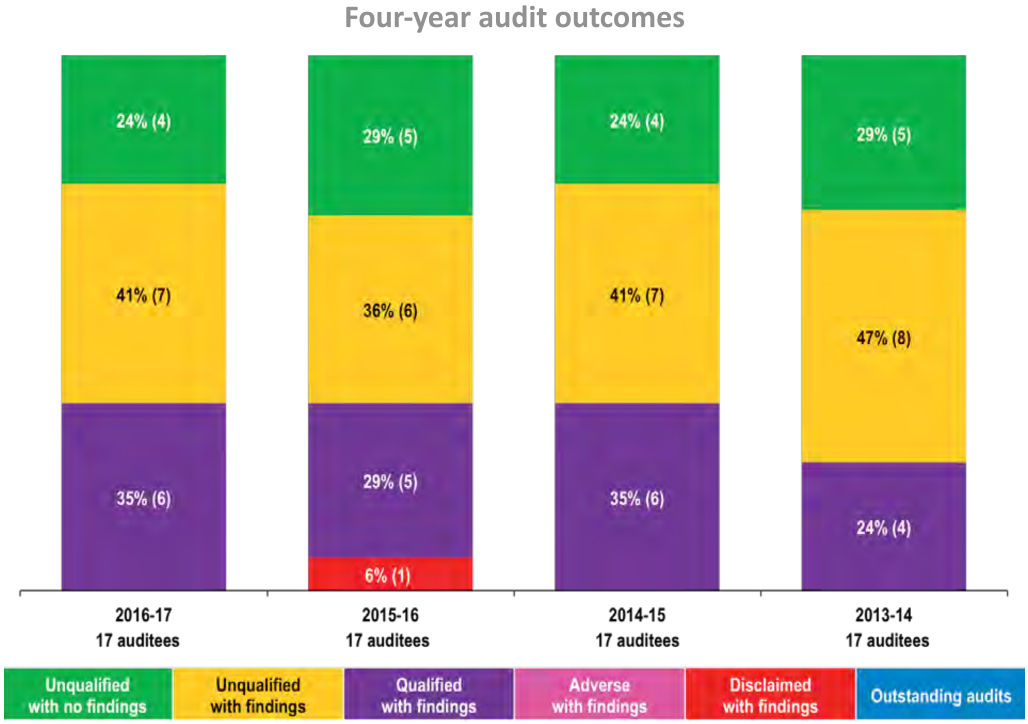
The audit outcomes in the province reflect little improvement over four years. The political leadership must set the tone and establish a strong accountability culture that positively influences the urgency with which key role players implement and monitor commitments, initiatives and consequence management.

Departments continued to experience challenges with the implementation of IT controls. Adequate progress was not made in addressing previous audit findings as well as new IT risks, as corrective measures were instituted late due to the required funding not being made available timeously. System functionality limitations as well as a moratorium on the hiring of staff resulted in a shortage of in-house IT skills for prolonged periods, which had a negative impact on IT controls.

The leadership must continue to lead the way and positively influence key role players to honour their commitments and institutionalise internal controls. Attention should be channelled towards the following important areas to effectively and positively reshape and promote the province to excel and build public confidence:

- Senior management should diligently implement and monitor action plans and recommendations to address previous years' audit findings.
- Basic key controls and monthly reporting processes, such as record management, key account reconciliations along with policy conformance, are the building blocks of internal control and require concerted and disciplined refinement, implementation and buy-in from all officials.
- The political and administrative leadership should ensure that competent people are employed in financial and SCM positions. These individuals should embrace accountability and take responsibility for their actions, coupled with a comprehensive understanding of key policies, processes and procedures.
- Frequent project planning, project management as well as monitoring and reporting on key priorities and service delivery attainments/backlogs are critical to enable swift intervention and management remediation.

16.6 Mpumalanga



The audit outcomes in Mpumalanga were inconsistent over the past four years with 65% of the auditees attaining unqualified audit outcomes during the 2016-17 financial year. Four auditees (24%) attained unqualified audit opinions with no findings, with three (18%) of these maintaining their clean administration status over the past four financial years. The driver of the good audit outcomes at the auditees with clean audits was mainly their prompt implementation of responsive action plans that were designed to address identified risk areas. In turn, these actions ensured a sound internal control environment. The overall provincial picture can change significantly if the other auditees also adopt these actions.

The audit outcome of one auditee, the Mpumalanga Economic Growth Agency, improved to a qualified audit opinion from a disclaimer in 2015-16. The entity took advantage of the interim audit to address some of the previous year's qualification areas and was also assisted by consultants to clean up the financial information, as the entity had not implemented basic daily and monthly disciplines. Work still needs to be done to improve other key elements of the entity's internal controls; moreover, the key processes need to be institutionalised to move the entity towards clean administration.

This slight improvement by the Mpumalanga Economic Growth Agency was, however, negatively offset by the regression of Social Development from a clean audit to an unqualified opinion with findings. During the 2016-17 financial year, the department decentralised the processes relating to the planning, collection, collation and reporting of performance information but did not properly institute the monitoring systems to respond to this change, hence the regression.

Similar to the previous year, six auditees (35%) could not adequately address significant errors identified in their financial statements, leading to qualified audit outcomes mainly in the areas of assets and revenue. We acknowledge the efforts by some of the auditees to improve audit outcomes, but unfortunately these efforts did not translate into tangible improvements due to significant weaknesses in the internal control environment as well as delays in finding practical solutions to recurring qualification areas. Culture, Sport and Recreation was further affected by instability in key positions, particularly at the level of chief financial officer. Furthermore, the review of the financial statements and performance reports by internal audit units, audit committees and the provincial treasury did not have the desired impact, as the underlying records supporting the financial statements contained errors.

The quality of financial statements and performance reports remains a matter of concern, with auditees still relying on the auditors to identify errors in the financial statements submitted for auditing. Eleven auditees (65%) received unqualified audit outcomes, but three (18%) received such outcomes only because they corrected all the material errors identified during the audit. In some instances, the root causes of the errors identified were similar to those that caused errors in previous years, indicating that these were not promptly addressed during the year. Overall, the province remained stagnant with no significant improvement in the audit outcomes, as there were still widespread weaknesses in the internal control environment.

We audited 17 key projects funded by conditional grants at six provincial departments and were encouraged that planned targets were achieved on 14 (82%) of these projects and that grants allocated were spent in accordance with the respective conditions. At the same time, we raised findings on non-compliance with SCM prescripts on three projects (18%) and identified accounting errors relating to capital expenditure and irregular expenditure on five projects (29%).

Accountability towards the timely discharge of commitments made by key stakeholders will help the province realise improvement in an otherwise stagnant environment.

Overall, the province still struggled to report reliable information on its predetermined objectives, as 12 auditees (71%) regressed in this area from the previous year due to a lack of proper review processes to ensure that reported information was credible. However, the discipline exercised by the province in the management and reporting of key projects funded by conditional grants set the proper platform for possible improvement on the planning, delivery and reporting of all other objectives contained in annual performance plans.

SCM continued to be a challenge and weaknesses in this area contributed to 94% of the total irregular expenditure (R3,2 billion) incurred in the financial year under review. Although the amount of irregular expenditure incurred in the current year had decreased, the province had not yet mastered the art of properly investigating irregular expenditure previously identified, as more than 70% of the current year's irregular expenditure arose from old multi-year contracts that had not been investigated. As a result, the closing balance of irregular expenditure increased to R11,2 billion (2015-16: R8,6 billion). Unauthorised expenditure increased to R98 million (2015-16: R9 million) due to Education overspending on programme 2: public ordinary schools education by R97 million. The reasons for the unauthorised expenditure included poorly prepared budgets. The political leadership should regularly monitor the progress and quality of investigations into previously reported instances of irregular and unauthorised expenditure to ensure that they are appropriately dealt with in line with legislation.

We noted a slight improvement in the financial health of the province, but some auditees still struggled with cash-flow management because of poor budget control and a lack of effective debt-management strategies. Consequently, these auditees failed to pay money owed within 30 days as required by legislation. Noticeable was also a trend by auditees to carry over their debt to the new budget. This had a negative impact on the delivery of planned targets in the new budget period. In addition, there was a concern about the financial independence of the two strategic public entities in the province, namely Mpumalanga Economic Growth Agency and Mpumalanga Tourism and Parks Agency. Both these entities depended largely on equitable share allocations as they were either not generating much income on their own or unable to collect amounts owed to them. The province is encouraged to monitor the implementation of the strategies in place to enable these entities to be self-sustainable to release much needed funds into the provincial fiscus to focus on service delivery.

In line with the previous year, IT controls in the province were fairly well managed at five auditees (29%) in support of their business objectives. This was due to a skilled workforce and management taking accountability to maintain good IT controls and addressing previous audit findings. Furthermore, oversight bodies such as the provincial government IT officers' council and internal audit units continued to play an important role in maintaining IT controls at all the auditees in the province. However, there were still some challenges in ensuring the effectiveness of IT governance controls (59%), security management controls (41%), and user access management controls (53%).

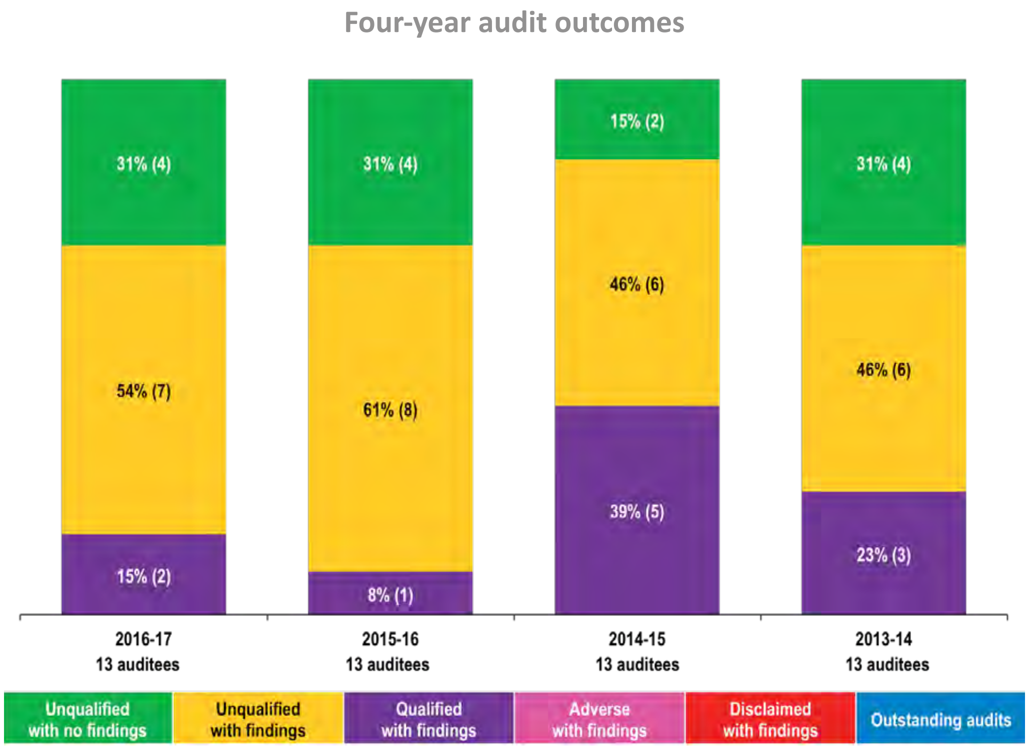
The effectiveness of the work performed by the various assurance providers, such as the internal audit unit, audit committee, provincial treasury and public accounts committee, was hampered significantly by management's failure to implement their recommendations or resolutions. In the last four financial years, we have consistently shared our key message on the actions needed to improve audit outcomes with accounting officers and authorities, members of the executive council, the premier and the legislature through our reports and interactions with them. In most cases, the engagements with the political leadership were well received and commitments to strengthen the key control environment and improve the audit outcomes were given.

We have continued to monitor these commitments and other initiatives of the executive and the legislature. Regrettably, the work done by the provincial leadership has not had the desired impact on the audit outcomes due to various challenges, including vacancies and instability in key positions, slow responses and a lack of consequence management for poor performance and transgressions. The province should focus on the following commitments to improve this situation:

- The legislature's commitment to track house resolutions and follow up implementation by auditees, which was still in progress.
- Commitments by executive authorities to closely monitor the performance of their departments, particularly SCM compliance.

We remain positive that should the weaknesses in the internal control environment be addressed, there will be a noticeable movement towards clean audits. As such, we will continue investing efforts in assisting the key role players to improve audit outcomes, mainly through our enhanced assessment of key controls and engaging the accounting officers, accounting authorities, audit committees and executive authorities on the status thereof.

16.7 Northern Cape



The Northern Cape provincial government consists of 20 auditees, including 13 departments and seven listed public entities. As part of our audit methodology, we classified these seven listed public entities as small auditees based on their importance and the size and nature of their business. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, it would have reflected an overall stagnation in 2016-17, with seven auditees (35%) receiving clean audit outcomes, nine auditees (45%) receiving unqualified opinions with findings, three auditees (15%) receiving qualified opinions, and one auditee (5%) whose audit was outstanding.

The four-year audit outcomes of the province showed a slight improvement, but the province slightly regressed when compared to the previous year. We complimented the three oversight departments (premier's office, provincial treasury and provincial legislature) in the previous year on achieving clean audits. In addition, Environment and Nature Conservation improved to a clean audit in the year under review. While we commend the oversight departments for again obtaining clean audits, we are concerned about the lack of improvement by most of the other departments. In addition, two of the largest budget spenders in the province (namely Health as well as Roads and Public Works), representing 39% of the provincial budget, received a qualified opinion in the year under review.

Health remained qualified over the past four years – with efforts by oversight structures and attention from the internal audit unit having little impact. Most qualification areas from the previous year were repeated, and we again identified material findings on the performance report and compliance. The department struggled with stability in key positions, including the position of accounting officer that was vacant for the last five months of 2016-17. The message of accountability should be emphasised and the leadership must deal decisively with those that do not follow policies and procedures. Additionally, a culture of discipline over internal controls and the proper monitoring of these should be implemented.

Oversight departments as well as the second and third levels of assurance providers have a role to play in directing departments towards improved audit outcomes. However, the responsibility for the implementation and monitoring of controls as well as keeping officials accountable remains that of the first level of assurance providers (accounting officer, senior management and executive authority).

The current audit outcomes reflect that these assurance providers were ineffective and that the message of accountability was not fully imbedded, as also reported in the previous year.

The financial audit areas of the two departments that were qualified related to correctly measuring and disclosing property, infrastructure and equipment as well as irregular expenditure. The number of qualifications on property, infrastructure and equipment increased from one department (8%) in 2015-16 to two departments (15%) in 2016-17, while the number of qualifications on irregular expenditure was unchanged at one department (8%).

The quality of financial statements submitted for auditing remains a major concern, with only seven departments (54%) submitting credible financial statements requiring no material adjustments during 2016-17 – the same as in the previous year. This confirms that many departments continued to experience difficulties with internal controls and relied too much on the audit process to detect misstatements in the financial statements and performance reports.

The slow response to recommendations and a lack of accountability are hindering improved audit outcomes and optimal service delivery to the citizens of the province.

The departments with no material findings on their performance reports improved year-on-year from seven (54%) in 2015-16 to nine (69%) in 2016-17. However, it is concerning that seven of the nine auditees were able to avoid findings on their performance reports by making material adjustments during the audit process. This shows that internal controls over the reporting of performance information still require attention.

The province struggled to improve its compliance with legislation and we did not raise findings in this area at only four departments (31%) (2015-16: four (31%). The non-adherence to SCM prescripts; the non-prevention of unauthorised, irregular and fruitless and wasteful expenditure; and the poor quality of financial statements submitted for auditing were the main contributors in this area. This was due to inadequate controls over monitoring compliance with legislation and a lack of timely, decisive action against transgressors.

Although irregular expenditure incurred decreased from R1,7 billion in the previous year to R1,6 billion in the year under review, the R10 billion closing balance of irregular expenditure is concerning. Health and Education were the highest contributors in the province with irregular expenditure of R574 million and R345 million, respectively. The most common areas of SCM non-compliance that caused irregular expenditure were procurement without competitive bidding or a quotation process and non-compliance with procurement process requirements.

SCM findings, allegations of financial misconduct and irregular expenditure should all be investigated. Irregular expenditure should only be written off after having been properly investigated. Of further concern is that no investigations into irregular expenditure incurred were carried out for the year under review at the top five contributors (Health; Education; Transport, Safety and Liaison; Cooperative Governance, Human Settlements and Traditional Affairs; and Roads and Public Works).

During the year under review, six departments either wrote off or condoned irregular expenditure of R92 million, but in no instance was any amount recovered from a liable person. The accounting officers should ensure that rigorous investigations are conducted and, where possible, the necessary steps are taken against the officials who caused the irregular expenditure.

While the financial health of the province stagnated, Health regressed to a state where material uncertainty existed regarding its financial health. This was due to increasing difficulties in recovering money owed to the department, concerns regarding the creditor-payment period, and a bank overdraft at year-end. Health also had a contingent liability for legal claims against the department amounting to R1,45 billion. We are concerned that the total current liabilities exceeded the total current assets at 11 departments (85%), while the cash shortfall as a percentage of the following year's total appropriation (excluding compensation of employees) of more than 10% was reported at six departments (50%). The practice of departments committing a substantial portion of the following year's budget in the current year is unsustainable and a concern that we also raised in the previous year. Budgetary controls need to be implemented in such a way that departments only spend what they budgeted for in a particular year. Where this is not done, departments should be called on to account for this.

As part of our evaluation of grant management, we audited 30 key projects at the 10 departments that received grants in terms of the Division of Revenue Act. We raised SCM findings relating to inadequate procurement processes by departments or implementing agents on 10 projects, while targets were also not achieved and/or evaluated at nine of these projects. Social Development underspent the substance abuse treatment grant by 100%, due to a dispute between the department and contractors relating to the construction of a substance abuse treatment centre in Kimberley. Health underspent the health facility revitalisation grant by 23%, due to delays in awarding tenders by implementing agents. We also raised concerns regarding the quality of workmanship relating to infrastructure development, and this had an impact on the time it took to complete facilities. These delays related mainly to poor project management and a lack of monitoring the progress on these projects. Where projects are delayed, it has a direct impact on service delivery – for which the responsible officials or service providers need to be held accountable.

The overall assessment of IT improved in the year under review although all departments still received findings in this area. As reported in the previous year, these findings can be attributed to concerns around IT managers not having adequate skills and resources to ensure that IT controls were adequately implemented. This resulted in most departments addressing symptoms rather than implementing processes that would improve the IT environment. Oversight bodies and the senior leadership of departments should intervene to ensure movement in this area.

The effectiveness of the work performed by the various assurance providers, such as the internal audit unit, audit committee and provincial treasury, was hampered by management's failure to implement their recommendations. Consequently, we identified a slow response in improving key controls and addressing recommendations as the key root cause that hindered progress in audit outcomes. This was worsened by accounting officers and senior management failing to keep officials accountable for their duties.

The commitments made by the premier in recent years focused on the implementation of consequences for poor performance as well as improving the quality of financial statements and the levels of compliance with legislation. These commitments were meant to improve the audit outcomes of departments, but as highlighted above, they were not implemented. The tracking of commitments remains a concern and we believe an improvement in the audit outcomes is possible if oversight structures frequently track their commitments. A lack of consequences by the political leadership at departments that did not improve their outcomes, especially in the area of compliance with key legislation, is one of the key reasons for the outcomes not improving.

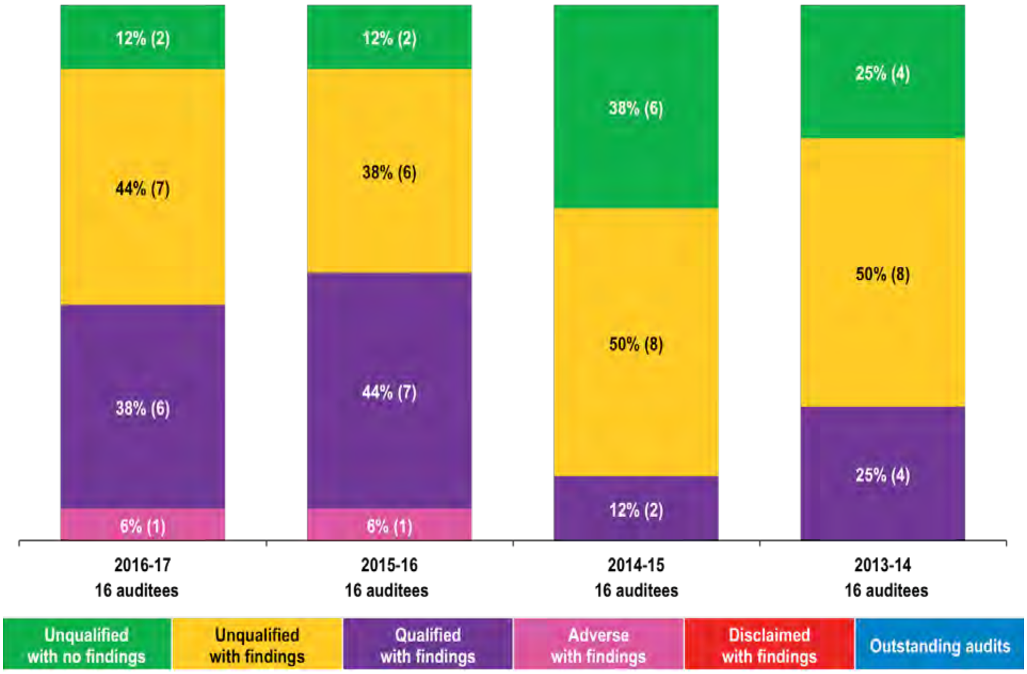
To further improve the audit outcomes, specifically at Health as well as Roads and Public Works, we recommend improvement in the monitoring of action plans as well as the implementation of reviews by internal audit units to confirm the status of action plans reported by senior management. Commitments made with regard to the resolutions of the public accounts committee need to be tracked and, at an overall level, accounting officers and executive authorities must hold staff accountable for transgressions.

The provincial government needs to prioritise accountability and the executive leadership needs to be held accountable for continued repeat audit findings if meaningful progress is to be made towards clean administration. This will require a combined effort by oversight bodies and the political leadership, and will result in improvements at departments that continue to struggle to report accurately on their financial and performance information and to comply with legislation.

A **lack of accountability and commitment towards clean administration was evident in the Free State and North West**. Their audit outcomes regressed over the four years – the Free State showed a slight improvement in 2016-17 but North West is in a downward spiral. The response by the provincial leadership was to contest the audit conclusions instead of addressing the weak control environment at most of the auditees.

16.8 Free State

Four-year audit outcomes



The Free State provincial government consists of 19 auditees, including 13 departments and six entities. As part of our audit methodology, we classified three entities as small auditees based on their role and size as well as the nature of their business. The audit outcomes of these entities are not included in this overview, but are published in the annexures available on our website. Overall, there was a regression in audit outcomes over the past four years. If the outcomes of these small auditees had been included, it would not have changed the picture as two entities received unqualified audit opinions with findings over the same period, while the audit outcome of one was still outstanding.

The provincial treasury improved from a qualified audit opinion to a clean audit and Health improved from a qualified opinion to an unqualified opinion with findings. The leadership at these departments responded to our messages and took timely action to address the previous year's qualifications. However, the premier's office, which should lead by example in the province, regressed from an unqualified opinion with findings to a qualified opinion and the Fleet Management Trading Entity regressed from a clean audit to an unqualified opinion with findings. The majority (63%) of auditees' audit outcomes stagnated on either an unqualified opinion with findings or a qualified opinion. Agriculture and Rural Development received an adverse opinion for the last two years. The lack of progress in the audit outcomes was attributable to the leadership's lack of focused and committed attention to continuously strengthen internal controls and improve the monitoring thereof. The provincial audit outcomes will not improve to the desired level if the right tone is not set at the top and the leadership does not take accountability to address the root causes of the audit findings to improve the control environment.

During 2015-16, we urged the political and administrative leadership to take accountability for and address the control weaknesses that resulted in a significant regression in audit outcomes. Five departments disputed these audit outcomes, which resulted in the late or non-tabling of their annual reports.
The leadership then committed that disputes would be resolved, the use of implementing agents would be reviewed with a view to eliminating this practice, and accounting officers would provide more assurance through oversight and taking ownership of the control environment. These commitments were not honoured as they only received attention close to the reporting date, resulting in limited progress being made to improve audit outcomes.

The slow response by the political and administrative leadership to honour their commitments and address the weak control environment, a lack of consequences and the continued disregard for compliance with legislation resulted in findings at 13 auditees and material adjustments to the financial statements being required at 10. Additionally, there was a noticeable regression in the quality of reported performance information as 10 auditees had material findings, compared to five in the previous year. This regression was mainly due to management not prioritising transparent reporting on the achievement of predetermined objectives. Instability and vacancies in key positions as well as inadequate documentation further contributed to the poor quality of reported performance information. IT remains critical for the integrity and availability of performance information to enable reliable reporting. However, there were no dedicated strategies to implement an IT platform for performance information.

Effective monitoring and oversight by all assurance providers are essential to break the cycle of impunity and improve internal controls. The administrative and political leadership should accept responsibility for their actions and should create a culture that will result in a responsive, accountable, effective and efficient provincial government as set out in the MTSF.

Irregular expenditure disclosed in the financial statements increased from R1,927 billion to R5,421 billion. This was mainly due to five departments reporting irregular expenditure to address the previous year's qualifications. However, the amount of R5,421 billion is understated, as Agriculture and Rural Development and the premier's office did not disclose irregular expenditure of R974 million and subsequently received a qualified audit opinion. The most common instances of irregular expenditure related to three quotations not being obtained, competitive bids not being invited, and the preference point system not being applied or being incorrectly applied. The main contributors to irregular expenditure were Health (R3,502 billion), Human Settlements (R1,015 billion) and Education (R680 million). The amount for Health is high as a result of the effort the department made to quantify its irregular expenditure and to deal with the previous qualification on irregular expenditure. The closing balance of irregular expenditure was R9,224 billion, which is an indication that irregular expenditure was not always investigated adequately to identify the officials to be held accountable for the possible recovery of losses, resulting in the year-on-year increase in the balance. Where irregular expenditure was investigated, officials were seldom found liable and amounts were written off. The leadership's involvement in the decision-making that led to transgressions resulted in their inability to hold staff accountable and, as a result, adequate consequence management processes were not implemented.

The departments' financial health continued to deteriorate with only the provincial treasury not requiring intervention. This was due to the provincial leadership not taking accountability to plan properly and considering the available budget when committing to strategic projects, so that funds were used optimally. Funds to be surrendered to the revenue fund and accruals and payables not recognised exceeded cash on hand by R2,6 billion. A significant portion of the 2017-18 budget would therefore be required to settle these obligations, reducing departments' ability to effectively deliver on their mandate. The intervention by the provincial treasury at Education since April 2015 had not improved financial management at the department, as it continued to incur irregular expenditure and to commit funds in excess of what would be available for future projects and services. Furthermore, Health is the defendant in lawsuits of R1,5 billion. Should these claims materialise, it could derail service delivery by this department as these were not budgeted for. The combined bank overdraft balances of Education and Health of R885 million put pressure on the entire province, as these departments are prioritised for funding. These signs of financial failure should receive urgent attention because without improved fiscal disciplines for the more effective, efficient and economical use of resources, the departments' financial health and service delivery will continue to deteriorate.

An important point in the MTSF is to establish an accountable, effective and efficient provincial government that promotes accountability for government spending of the budget in a manner that will have a positive impact on people's lives. At Agriculture and Rural Development as well as Education, however, grants were not used for their intended purpose, and Education underspent conditional grants by R203 million, resulting in the public not receiving services as outlined in these departments' annual performance plans.

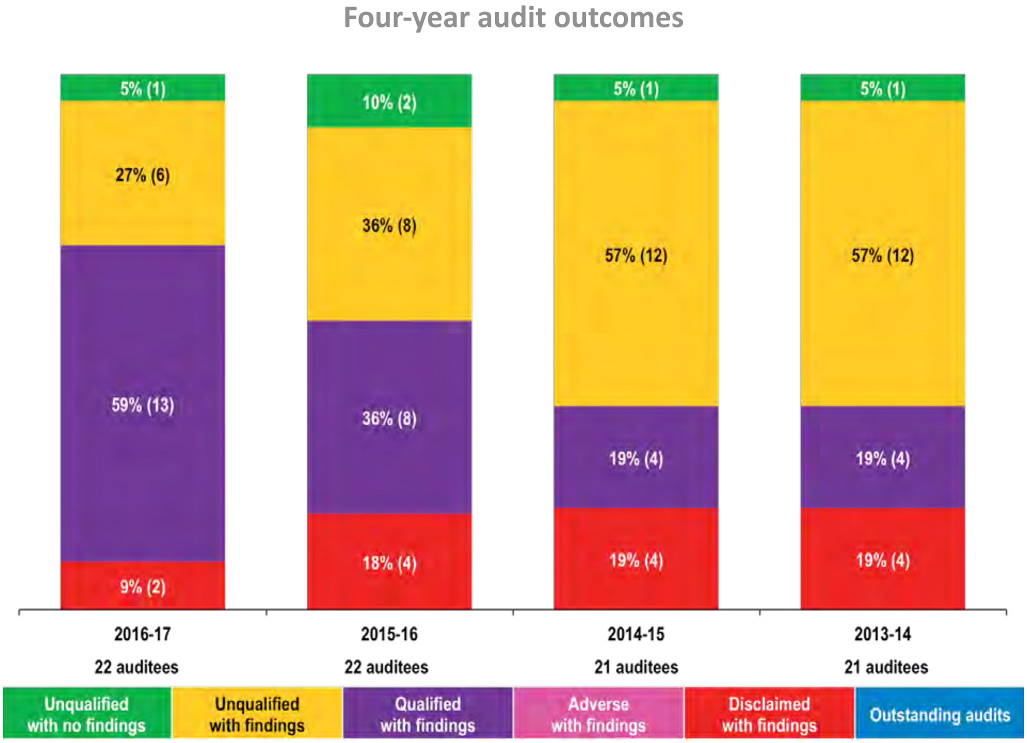
Spending on key projects was riddled with shortcomings, as the departments did not always apply the principles of sound project planning and management, resulting in cost overruns, poor quality workmanship, delays in the completion of projects, and potential fruitless and wasteful expenditure. Consequently, key performance targets were not always achieved. The provincial leadership continued to make use of implementing agents to deliver some key projects without ensuring that they complied with SCM requirements. We are concerned about the continuous disregard for procurement processes by the administrative and political leadership that resulted in irregular expenditure, coupled with limited consequences for these transgressions, as it created an environment conducive to misappropriation, wastage and abuse of state funds.

The construction of a district hospital and a psychiatric complex by Health had been placed on hold since 2012 due to a lack of funding. These delays affected service delivery and may result in additional costs due to changes in the community's needs and technological advancements. In spite of Health's cash-flow challenges, it irregularly awarded a tender to a service provider for the procurement of buses to be utilised as mobile clinics. We noted concerns regarding the department not applying the preferential procurement requirements, specifically with regard to the assessment of functionality to disqualify certain bidders as well as awarding points for local content.

There were significant delays in the construction of a school where the contract was ceded to a second contractor after 29 months due to poor performance with only 33% of the work having been completed. The initially planned project duration was 16 months. The quality of most of the structures was poor and had to be demolished or corrected. In another instance, a school was completed but the building was of sub-standard quality due to poor workmanship. The project was also not properly planned, as there were only enough learners to fill six of the 29 classrooms built. Public Works and Infrastructure was the implementing agent for both projects and had certified to Education that the work performed by the contractors was satisfactory and that payments could be made.

Effective monitoring and oversight by all assurance providers are essential to break the cycle of impunity and improve internal controls. The administrative and political leadership should accept responsibility for their actions and should create a culture that will result in a responsive, accountable, effective and efficient provincial government as set out in the MTSF. Mechanisms to promote accountability typically include basic daily and monthly checks and balances on compliance, financial and performance information; managing the performance of staff; and implementing consequences for poor performance and transgressions. Accountability and transparency are considered the main pillars of good governance and sustainable clean audits will only be achieved through a strong foundation of good governance.

16.9 North West



The North West provincial government consists of 36 auditees, being 13 departments and 23 entities. As part of our audit methodology, we classified 14 entities as small or dormant auditees based on their importance and the size and nature of their business. The audit outcomes of these entities are not included in this overview but are published in the annexures available on our website. If these small auditees had been included in the overall audit outcomes, the picture for 2016-17 would have further regressed, with one auditee (3%) receiving a clean audit outcome, nine auditees (25%) unqualified opinions with findings, 17 auditees (47%) qualified opinions with findings, and four auditees (11%) disclaimed opinions. The 2013-14 audit outcome of the former Department of Human Settlements is included in the four-year audit outcome figure for comparative purposes.

Of specific concern is the audit outcome of the premier's office, which has remained qualified for the last two years with increasing irregular expenditure. As a key monitoring and oversight department, the premier's office should set an example of good governance and accountability. The lack of improvement in audit outcomes indicates that the provincial executive leadership was not interested in our messages and that, overall, there were poor accountability and consequence management. Specific commitments made relating to accountability and consequence management had not been successfully implemented. A consequence management committee had still not been established, resulting in the provincial executive leadership not holding accounting officers or accounting authorities accountable for the lack of progress made over the four-year period. Focused political will and a considerable investment in monitoring and oversight are required to turn around the audit outcomes of the province and create a baseline from which accountability can be inspired and strengthened.

The slow response by management to address root causes and the lack of consequence management for continued transgressions and poor performance should have been the priority of the provincial executive leadership, as highlighted in the previous year's general report. Contrary to this and irrespective of the continued reinforcement of our messages, the overall audit outcomes of North West regressed over the last four years with only 32% of the auditees obtaining

Accountability, consequence management and action by the provincial executive leadership in addressing root causes, are the cornerstones to improving audit outcomes.

financially unqualified opinions in 2016-17 compared to 46% in 2015-16 and 62% in 2014-15 and 2013-14. Most of the audit findings were repetitive in nature with auditees focusing on disagreeing with findings and questioning audit processes instead of finding a way forward to address the matters raised in audit reports. Finance was the only department that maintained its audit outcome of financially unqualified with no other findings for four consecutive years. Unfortunately, the coordinating role of the department was hampered by other auditees not being responsive to its recommendations and the best practices consequently not being replicated. The outcomes of the public entities in the province further regressed, with no public entity achieving a financially unqualified opinion in 2016-17.

The most common compliance finding related to financial statements containing material misstatements. The submission of quality financial statements for auditing within the legislated timelines and the availability of the underlying financial records remain a concern, with auditees relying on the audit process to produce credible financial statements. This resulted in 109 material adjustments (an average of five per auditee) being required during the audit process to correct these misstatements. Had these adjustments not been allowed, only two auditees (9%) would have received unqualified opinions as opposed to the reported seven (32%). Vacancies in key positions and the lack of appropriate competencies were again the main reasons for auditees' inability to implement basic controls such as record management as well as daily and monthly reconciliations to ensure the preparation of reliable financial reports. This also contributed to an over-reliance on consultants, specifically at public entities. An intensive effort is required to ensure stability and appropriate competencies in key positions, as this is crucial in institutionalising key controls that will address identified weaknesses.

Overall, 91% of the auditees had material findings on their performance reports. The most common findings related to indicators that were not well defined and reported achievements that were not supported by source documents due to poor record keeping and ineffective systems and processes to enable reliable reporting. IT remains critical to enable accurate reporting, enhance service delivery and promote effective oversight. Although departments made some progress in addressing weaknesses in IT controls identified in the previous year, public entities did not make any progress. This could result in disruptions in operations and increase the risk of fraudulent transactions that could result in financial losses. The government IT officer and the coordinating departments need to ensure that specific attention is given to assist the province in this regard.

Most auditees (91%) still had findings on compliance with legislation, specifically in the areas of irregular expenditure and non-adherence to procurement and contract management prescripts, which also resulted in an increase in the irregular expenditure incurred from R3 billion in 2015-16 to R3,6 billion in 2016-17. As a result of this year-on-year increase and due to irregular expenditure not being investigated, the total unresolved balance for the province was R16,5 billion. A total of 59% of the irregular expenditure was incurred by the following top three contributors in 2016-17: Community Safety and Transport Management (R880 million), Health (R714 million), and Public Works and Roads (R550 million).

The use of implementing agents at the premier's office and Rural, Environmental and Agricultural Development resulted in irregular expenditure, as the implementing agents did not adhere to the departments' SCM policies, as required. There were also instances where management applied discretion to deviate from SCM processes without adequate reasons, such as the awarding of a tender for the rehabilitation of flood-damaged roads of R103 million at Public Works and Roads; and the awarding of various cluster security contracts to suppliers not recommended by the department's bid adjudication committee at Health. A provincial committee to advise auditees on dealing with irregular expenditure was established in February 2017, but to date the submissions by departments have not been adequate to assist in clearing the growing irregular expenditure. In addition, the legislature's portfolio committees and the public accounts committee also did not have much of an impact on the lack of accountability and consequence management in the province.

We audited 16 key projects funded by conditional grants. Although 95% of the total grant allocation of R7 139 million received by the province was spent during the year, we identified instances where targets of key projects were not achieved or where work was not completed at the desired quality. For example, at Education and Sport Development, completed schools were not properly commissioned, including toilets that were not working and roofing of schools that had been poorly installed. At Local Government and Human Settlements, a housing project was delayed for over 20 months and fruitless and wasteful expenditure was incurred, as 503 housing units had to be demolished and rebuilt due to quality defects, despite the contractor having been paid in full. The root cause of these findings was poor project management. Had the departments adequately monitored the work and progress by contractors before payments were made, these defects could have been identified and addressed. Government spending without ensuring value for money is of particular concern, taking into account the increased financial pressure on auditees to make sound financial decisions and implement cost-containment measures to ensure financial viability.

The outcomes of the public entities in the province remained poor over the four years with a regression in 2016-17, with no public entity achieving a financially unqualified opinion. In the previous year, we reported that the processes and legislative requirements to restructure certain public entities needed to be finalised. No progress had been made in this regard, however, as the implementation of decisions was emphasised without ensuring that the appropriate legislative approvals were obtained. We remain concerned that the provincial executive leadership did not have a complete picture of all the entities in the province. This resulted in a lack of governance at the entities, while the departments responsible for these entities did not monitor them appropriately. This is evident from the number of entities operating without approved budgets and without reporting quarterly and annually on their performance.

The financial health of most public entities in the province remains the biggest concern. Most entities continued to incur deficits every year, while the total current liabilities exceeded the total current assets at seven entities (78%). This indicates that the entities could not honour their liabilities and were therefore fully dependent on funding from their holding companies or departments to continue to operate as going concerns. The financial statements of two entities were so poor that a reliable assessment could not be done, but there were indicators of financial problems. While the financial health of departments improved over the four-year period, there was still a concern regarding accruals outstanding in excess of 30 days at seven departments (54%), which indicates that suppliers were not paid timeously. The non-payment of suppliers on a timely basis, specifically by Health, Education and Public Works and Roads, severely affected service delivery. In addition, litigation and claims against Health in excess of R1,2 billion highlight the department's and province's financial vulnerability should these claims be successful. Strong financial discipline is required to manage, monitor and spend funds to ensure the most effective, efficient and economical use of resources.

The province's downward spiral will continue until such time as the pillars of accountability and good governance are put in place. Consequently, the provincial executive leadership and oversight structures should aspire to develop a comprehensive assurance model, including strong and effective governance structures, which is required so that all key role players adequately perform their monitoring duties and the administrative leadership is held accountable for future commitments with regard to improved financial and performance reporting disciplines. This should include key oversight activities, especially on matters of consequence management, the tracking of commitments, the implementation of audit action plans, and the timely tabling and regular follow-up of key resolutions. In addition, the provincial leadership should take responsibility for creating a culture in which accountability can be restored and strengthened in the province.

17 Need to know

17.1 Our audit process and focus

What is our audit and reporting process?

We audit every department and some of the public entities in the country (also called auditees in this report) to report on the quality of their financial statements and performance reports and on their compliance with key legislation.

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

- We report our findings, the root causes of such findings and our recommendations in **management reports** to the senior management and accounting officers or authorities of auditees, which are also shared with the ministers, members of the executive councils and audit committees.
- Our opinion on the financial statements, material findings on the performance reports and compliance with key legislation, as well as significant deficiencies in internal control, 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 **consolidated report** (such as this one), in which we also analyse the root causes that need to be addressed to improve audit outcomes. Before the general report is published, we share the outcomes and root causes with the national and provincial leadership, Parliament and the legislatures, as well as key role players in national and provincial government.

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

During the audit process, we work closely with accounting officers or authorities, senior management, audit committees and internal audit units, as they are **key role players** in providing assurance on the credibility of the auditees' financial statements and performance reports as well as on their compliance with legislation.

We also continue to strengthen our relationship with the coordinating and monitoring departments (such as the treasuries, premier's offices and the DPME) as well as Parliament and provincial legislatures, as we are convinced that their involvement and oversight have played – and will continue to play – a crucial role in the performance at departments and public entities. We share our messages on key controls, risk areas and root causes with them, and obtain and monitor their commitments to implementing initiatives that can improve audit outcomes.

The overall audit outcomes fall into five categories:

1. Auditees that receive a **financially unqualified opinion with no findings** are those that are able to:
   - produce financial statements free of 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 line with the predetermined objectives in their annual performance plan, and in a manner that is useful and reliable
   - comply with key legislation.

   This audit outcome is also commonly referred to as a 'clean audit'.
2. Auditees that receive a **financially unqualified opinion with findings** are those that are able to produce financial statements without material misstatements, but are struggling to:
   - align their performance reports to the predetermined objectives to which they have committed in their annual performance plans

- set clear performance indicators and targets to measure their performance against their predetermined objectives
- report reliably on whether they have achieved their performance targets
- determine which legislation they should comply with, and implement the required policies, procedures and controls to ensure that they comply.

3. Auditees that receive a **financially qualified opinion with findings** face the same challenges as those that are financially unqualified with findings in the areas of reporting on performance and compliance with key legislation. In addition, they are unable to produce credible and reliable financial statements. Their financial statements contain misstatements that they cannot correct before the financial statements are published.
4. The financial statements of auditees that receive an **adverse opinion with findings** include so many material misstatements that we disagree with virtually all the amounts and disclosures in the financial statements.
5. Those auditees with a **disclaimed opinion with findings** cannot provide us with evidence for most of the amounts and disclosures in the financial statements. We are therefore 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 performance reports
   - not complying with key legislation.

What is the purpose of the annual audit of the 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 reporting framework and applicable legislation. The audit provides the users with reasonable assurance regarding the degree to which the financial statements are reliable and credible on the basis that the audit procedures performed did not reveal any material errors or omissions in the financial statements. We use the term 'material misstatement' to refer to such material errors or omissions.

We report the **poor quality of the financial statements** we receive in the audit reports of some auditees as a material finding on compliance, as it also constitutes non-compliance with the PFMA. The finding is only reported for auditees that are subject to the PFMA and if the financial statements we receive for auditing include material misstatements that could have been prevented or detected if the auditee had an effective internal control system. We do not report a finding if the misstatement resulted from an isolated incident or if it relates to the disclosure of unauthorised, irregular or fruitless and wasteful expenditure identified after the financial statements had been submitted.

What does compliance with key legislation mean?

We annually audit and report on **compliance by auditees with key legislation** applicable to financial and performance management and related matters. We focus on the following areas in our compliance audits, if they apply to the particular auditee: ■ the quality of financial statements submitted for auditing ■ asset and liability management ■ budget management ■ expenditure management ■ unauthorised, irregular and fruitless and wasteful expenditure ■ consequence management ■ revenue management ■ strategic planning and performance management ■ financial statements and annual report ■ transfer of funds and conditional grants ■ procurement and contract management (in other words, SCM).

In our audit reports, we report findings that are material enough to be brought to the attention of auditee management, as well as oversight bodies and the public.

What is the scope of supply chain management audits?

We test whether the **prescribed procurement processes have been followed** to ensure that all suppliers are given equal opportunity to compete and that some suppliers are not favoured above others. The principles of a fair, equitable, transparent, competitive and cost-effective SCM process are fundamental to the procurement practices of the public sector, as enshrined in the country's constitution and prescribed in the PFMA and its regulations. The PFMA and these regulations define what processes should be followed to adhere to the constitutional principles, the level of flexibility available, and the documentation requirements.

We also focus 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 assess the **financial interests of employees of the auditee and their close family members** in suppliers to the auditee. Although there is no legislation that prohibits making awards to suppliers in which state officials have an interest, the **amended Public Service Regulations prohibit employees of departments from doing business with the state** from 1 August 2016. The regulations allowed employees that were doing business with the state on 1 August 2016 time until February 2017 to stop the business or resign as an employee.

What is irregular expenditure?

Irregular expenditure is expenditure that was **not incurred in the manner prescribed by legislation**; in other words, somewhere in the process that led to the expenditure, the auditee did not comply with the applicable legislation.

Such expenditure does **not necessarily mean that money had been wasted or that fraud had been committed**. It is an indicator of non-compliance in the process that needs to be investigated by management to determine whether it was an unintended error, negligence or done with the intention to work against the requirements of legislation (which, for example, require that procurement should be fair, equitable, transparent, competitive and cost-effective).

Through such **investigation**, it is also determined who is responsible and what the impact of the non-compliance is. Based on the investigation, the next steps are determined. One of the steps can be condonement if the non-compliance had no impact and negligence was not proven. Alternatively, if negligence was proven, the steps can be disciplinary steps, the recovery of any losses from the implicated officials or even cancelling a contract or reporting it to the police or an investigating authority.

The PFMA is clear that **accounting officers and authorities are responsible** for preventing irregular expenditure as well as on what process to follow if it has been incurred.

In order to promote transparency and accountability, auditees **should disclose all irregular expenditure identified (whether by the auditee or through the audit process)** in their financial statements with detail on how it had been resolved; in other words, how much had been investigated, recovered or condoned.

What is fruitless and wasteful expenditure?

Fruitless and wasteful expenditure is expenditure that was made in vain and that could have been avoided had reasonable care been taken. This includes penalties and interest on the late payment of creditors or statutory obligations as well as payments made for services not used or goods not received.

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

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

What is unauthorised expenditure?

Unauthorised expenditure refers to expenditure that auditees incurred without provision having been made for it in the approved budget.

The PFMA requires accounting officers to take all **reasonable steps to prevent unauthorised expenditure**. Auditees should have processes to identify any unauthorised expenditure 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.

What are conditional grants?

Conditional grants are **funds allocated from national government to provincial departments**, subject to certain **services being delivered or on compliance with specified requirements**.

Conditional grant allocations are approved each year through the Division of Revenue Act. This act indicates the approved allocation per auditee for that particular year, together with a forward estimate for the next two years.

Conditional grants stem from government's vision and priorities as articulated in the MTSF, which focuses on placing the economy on a qualitatively different path that ensures rapid sustainable growth, higher investments, increased employment, reduced inequality and the deracialisation of the economy.

In support of these goals, conditional grants are provided to provincial departments to:

- reduce the concentration of people in urban areas (comprehensive agricultural support programme grant and human settlements development grant)
- increase adequate infrastructure (education infrastructure grant, provincial roads maintenance grant and health facility revitalisation grant)
- improve skills (HIV and Aids grant, expanded public works programme integrated grant for provinces and social sector expanded public works programme incentive grant for provinces).

During our audits, we test compliance with the Division of Revenue Act and the individual grant frameworks, as well as the achievement of planned targets for selected projects or programmes funded by each grant allocation.

What is the purpose and nature of the annual audit of the 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 as defined in their annual performance plan, and to report on this in their performance reports.

On an annual basis, we audit **selected material programmes** of departments and objectives of public entities to determine whether the information in the performance reports is useful and reliable enough to enable 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 delivery by the auditee on its mandate. In the audit report, we report findings that are material enough to be brought to the attention of these users.

As part of the annual audits, we audit the **usefulness of the reported performance information** to determine whether it is presented in the annual report in the prescribed manner and is consistent with the auditee's planned objectives as defined in strategic and annual performance plans. We also assess whether the performance indicators and targets set to measure the achievement of the objectives are well defined, verifiable, specific, time bound, measurable and relevant.

We further audit the **reliability of the reported information** to determine whether it can be traced back to the source data or documentation and whether it is accurate, complete and valid.

When is human resource management effective?

HR management refers to the **management of an auditee's employees or human resources**. HR management is effective if adequate and sufficiently skilled staff members are in place and if their performance and productivity are properly managed.

Our audits include an assessment of HR management, focusing on the following areas: ■ HR planning and organisation ■ management of vacancies ■ appointment processes ■ performance management ■ acting positions ■ management of leave and overtime.

Our audits further look at the management of vacancies and stability in key positions, the competencies of key officials, performance management as well as consequences for transgressions, as these matters directly influence the quality of auditees' financial and performance reports and their compliance with legislation.

Based on the results of these audits, we assess the status of auditees' HR management controls.

When are internal controls effective and efficient?

A key responsibility of accounting officers, senior managers and officials is to **implement and maintain effective and efficient systems of internal control**.

We assess the internal controls to determine the effectiveness of their design and implementation in ensuring reliable financial and performance reporting and compliance with legislation. This consists of all the policies and procedures implemented by 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. To make it easier to implement corrective action, we categorise the principles of the different components of internal control under leadership, financial and performance management, or governance. We call these the drivers of internal control.

The key basic controls that auditees should focus on are outlined below.

Providing effective leadership

In order to improve and sustain audit outcomes, auditees require **effective leadership** that is based on a culture of honesty, ethical business practices and good governance to protect and enhance the interests of the auditee.

Audit action plans to address internal control deficiencies

Developing and monitoring the implementation of action plans to address identified internal control deficiencies are key elements of internal control, which are the responsibility of heads of departments, chief executive officers and their senior management team.

Some of the matters requiring attention include the following:

- Setting action plans to specifically address the external and internal audit findings.
- Assigning clear responsibility to specific staff to carry out action plans.
- Monitoring the audit action plan to ensure that the responsibilities assigned are carried out effectively and consistently.
- Developing audit action plans early enough in the financial year to resolve matters by year-end.

Proper record keeping and document control

Proper and timely record keeping ensures that **complete, relevant and accurate information** is accessible and available to support financial and performance reporting. Sound record keeping will also enable senior management to hold staff accountable for their actions. A lack of documentation affects all areas of the audit outcomes.

Some of the matters requiring attention include the following:

- Establishing proper record keeping so that records supporting financial and performance information as well as compliance with key legislation can be made available when required for audit purposes.
- Implementing policies, procedures and monitoring mechanisms to manage records, and making staff members aware of their responsibilities in this regard.

Implement controls over daily and monthly processing and reconciling of transactions

Controls should be in place to ensure that **transactions are processed accurately, completely and timeously**, which in turn will reduce errors and omissions in financial and performance reports.

Some of the matters requiring attention include the following:

- Daily capturing of financial transactions, supervisory reviews of captured information, and independent monthly reconciliations of key accounts.
- Collecting performance information at intervals appropriate for monitoring, setting service delivery targets and milestones, and validating recorded information.
- Confirming that legislative requirements and policies have been complied with before initiating transactions.

Review and monitor compliance with legislation

Auditees need to have mechanisms that can **identify applicable legislation as well as changes to legislation**, assess the requirements of legislation, and implement processes to ensure and monitor compliance with legislation.

What is information technology and what are information technology controls?

IT refers to the computer systems used for recording, processing and reporting financial and non-financial transactions. IT controls ensure the confidentiality, integrity and availability of state information, enable service delivery, and promote national security. Good IT governance, effective IT management and a secure IT infrastructure are therefore essential.

During our audits, we assess the IT controls that focus on IT governance, security management, user access management and IT service continuity – these are discussed on the following page.

To evaluate the status of the IT controls in the areas we audit, we group them into the following three categories, with reference to the control measures that should be in place:

1. **Where IT controls are being designed**, management should ensure that the controls would reduce risks and threats to IT systems.
2. **Where IT controls are being implemented**, management should ensure that the designed controls are implemented and embedded in IT processes and systems. Particular attention should be paid to ensuring that staff members are aware of and understand the IT controls being implemented, as well as their roles and responsibilities in this regard.

3. **Where IT controls have been embedded and are functioning effectively**, management should ensure that the IT controls that have been designed and implemented are functioning effectively at all times. Management should sustain these IT controls through disciplined and consistent daily, monthly and quarterly IT operational practices.

Information technology governance

IT governance refers to the leadership, organisational structures and processes which ensure that the auditee's IT resources will sustain its business strategies and objectives. Effective IT governance is essential for the overall well-being of an auditee's IT function and ensures that the auditee's IT control environment functions well and enables service delivery.

Security management

Security management refers to the controls preventing unauthorised access to the computer networks, computer operating systems and application systems that generate and prepare financial and performance information.

User access management

User access controls are measures designed by business management to prevent and detect the risk of unauthorised access to, and the creation or amendment of, financial and performance information stored in the application systems.

Information technology service continuity

IT service continuity controls enable auditees to recover within a reasonable time the critical business operations and application systems that would be affected by disasters or major system disruptions.

What are root causes?

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

Our audits include an **assessment of the root causes of audit findings**, based on the identification of internal controls that have failed to prevent or detect the error in the financial statements and performance reports or that have led to non-compliance with legislation. These root causes are confirmed with management and shared in the management report with the accounting officer and the executive authorities. We also include the root causes of material findings reported as internal control deficiencies in the audit report, classified under the key drivers of leadership, financial and performance management, or governance.

Who provides assurance?

Ministers, members of the executive councils and accounting officers use the **annual report** to report on the financial position of auditees, their performance against predetermined objectives and overall governance; while one of the important **oversight functions of legislatures is to consider auditees' annual reports**. To perform their oversight function, they need assurance that the information in the annual report is credible. To this end, the annual report also includes our audit report, which provides assurance on the credibility of the financial statements, the performance report and the auditee's compliance with legislation.

Our reporting and the oversight processes reflect on history, as they take place after the financial year. Many other role players contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.

The mandates of these role players differ from ours, and we have categorised them as follows:

- Those directly involved in the management of the auditee (management or leadership assurance).
- Those that perform an oversight or governance function, either as an internal governance function or as an external monitoring function (internal independent assurance and oversight).
- The independent assurance providers that give an objective assessment of the auditee's reporting (external independent assurance and oversight).

We **assess the level of assurance** provided by the role players based on the **status of auditees' internal controls and the impact of the different role players on these controls**. In the current environment, which is characterised by inadequate internal controls, corrected and uncorrected material misstatements in financial and performance information, and widespread non-compliance with legislation, all role players need to provide an extensive level of assurance.

What is the role of each key role player in providing assurance?

Senior management

Senior management, which includes the chief financial officer, chief information officer and head of the SCM unit, provides assurance by implementing the following basic financial and performance controls:

- 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.
- Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information.
- Review and monitor compliance with applicable legislation.
- Design and implement formal controls over IT systems.

Accounting officers or accounting authorities

While we recognise that accounting officers and authorities depend on senior management for designing and implementing the required financial and performance management controls, they are responsible for creating an environment that helps to improve such controls.

The responsibilities of accounting officers and authorities are clearly described in section 38 (for departments) and section 51 (for public entities) of the PFMA. This includes their responsibility to ensure that:

- there are consequences for transgressions through disciplinary steps against officials who contravene the PFMA and make or permit unauthorised, irregular and fruitless and wasteful expenditure
- appropriate, efficient and effective systems or policies are implemented and maintained for, among other, internal control, internal audit and SCM
- resources are used effectively, efficiently, economically and transparently
- effective and appropriate steps are taken to collect all money due to the auditee

- assets and liabilities are properly managed, including the safeguarding thereof
- expenditure is in accordance with the budget (including steps to prevent overspending).

Executive authorities

The executive authorities (ministers and members of the executive councils) have specific monitoring and oversight responsibilities in their portfolios in terms of the PFMA and the Public Service Act. They are well placed to bring about improvements in the audit outcomes by becoming more actively involved in key governance matters and by managing the performance of the accounting officers and authorities.

We are convinced that the oversight and monitoring roles of the executive strengthen the assurance processes significantly, and this has had a positive impact on the audit outcomes in the past year. We therefore undertake to carry on with our engagements with them, but with greater emphasis on quality conversations that will yield a stronger impact.

Internal audit units

The 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. The establishment of internal audit units is a requirement of legislation.

Audit committees

An audit committee is an independent body, created in terms of legislation, which advises the accounting officer or authority, senior management and executive authorities on matters such as internal controls, risk management, performance management and compliance with legislation. The committee is further required to provide assurance on the adequacy, reliability and accuracy of financial and performance information.

Coordinating or monitoring departments

At national and provincial level, some departments play a coordinating and monitoring role as defined in legislation and in their mandates, which should contribute to the overall assurance process. These departments are the National Treasury, provincial treasuries, offices of the premier and the DPME. We assess the impact of these departments on the controls of the auditees based on our interactions with them, commitments given and honoured as well as the impact of their actions and initiatives.

Public accounts committees and portfolio committees

Parliament and the provincial legislatures have a constitutional mandate to oversee executive action and ensure compliance with legislation. These institutions conduct oversight through committees established in line with the rules of Parliament and the provincial legislatures. Portfolio committees are required to assess the strategic and annual performance plans of departments and public entities to effectively fulfil their oversight role.

Informed by our constitutional mandate, we enable oversight, accountability and governance in the public sector through our regular engagements with Parliament and the provincial legislatures. We do this through oversight leadership and portfolio committee engagements, during which we present and discuss key controls and compliance findings arising from the audit process and the related root causes. The discussions include our recommendations on focus areas that require oversight intervention. We hope that through these interactions, specific oversight efforts will lead to improved governance and accountability in the public sector.

17.2 Glossary of key terminology used in this report

Asset (in financial statements)	Any item belonging to the auditee, including property, infrastructure, equipment, cash, and debt due to the auditee.
Backup (IT)	A backup, or the process of backing up, refers to the copying and archiving of computer data so that it may be used to restore the original after a data loss event. The primary purpose of a backup is to recover data after its loss, be it by data deletion or corruption.
Business continuity plan (BCP) (IT)	A business continuity plan is a plan to continue operations if an auditee is affected by different levels of disaster, which can be localised short-term disasters, to days-long building-wide problems, to a permanent loss of a building. Such a plan typically explains how the auditee would recover its operations or move operations to another location after damage by events like natural disasters, theft or flooding. For example, if a fire destroys an office building or data centre, the people and auditee or data centre operations would relocate to a recovery site.
Cash flow (in financial statements)	The flow of money from operations: incoming funds are revenue (cash inflow) and outgoing funds are expenses (cash outflow).
Chief information officer or government information technology officer (IT)	The most senior official of the auditee who is accountable for aligning IT and business strategies; for planning, resourcing and managing the delivery of IT services and information; and for the deployment of associated human resources. The chief information officers in the South African public sector are referred to as government information technology officers. The position was established by a cabinet memorandum in 2000.
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.
Configuration (IT)	The complete technical description required to build, test, accept, install, operate, maintain and support a system.
Creditors	Persons, companies or organisations to whom the auditee owes money 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 within 12 months. All other assets are classified as non-current, and typically include property, plant and equipment as well as long-term investments.
Current liability (in financial statements)	Money owed by the auditee to companies, organisations or persons who have supplied goods and services to the auditee.

Disaster recovery plan (DRP) (IT)	A disaster recovery plan is a documented process or set of procedures to recover and protect an auditee's IT infrastructure in the event of a disaster. Usually documented in written form, the plan specifies the procedures that an auditee is to follow in the event of a disaster. It is a comprehensive statement of consistent actions to be taken before, during and after a disaster. The disaster could be natural, environmental or man-made. Man-made disasters could be intentional (e.g. the act of an attacker) or unintentional (i.e. accidental, such as the wall of a man-made dam breaking).
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 processing and reconciling transactions, the preparation of regular and credible financial and performance reports as well as the review and monitoring of compliance with key legislation.
Firewall (IT)	A security system used to prevent unauthorised access between networks (both internal/internal and internal/external). A firewall will allow only approved traffic in and/or out by filtering packets based on source/destination. The firewall inspects the identification information associated with all communication attempts and compares it to a rule set consistent with the auditee's security policy. Its decision to accept or deny the communication is then recorded in an electronic log.
Going concern	The presumption that an auditee will continue to operate in the near 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.
Implementing agent	Government institutions (e.g. the Independent Development Trust), non-governmental organisations or private sector entities appointed by the auditee to manage, implement and deliver on projects.
IT infrastructure (IT)	The hardware, software, computer-related communications, documentation and skills that are required to support the provision of IT services, together with the environmental infrastructure on which it is built.
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).

Material finding (from the audit)	An audit finding on the quality of the performance report or compliance with key legislation that is significant enough in terms of either its amount or its nature, or both these aspects, to be reported in the audit report.
Material misstatement (in financial statements or performance reports)	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 financial statements or performance reports)	Incorrect or omitted information in the financial statements or performance report.
Patch management (IT)	A piece of programming code that is added to an existing program to repair a deficiency in the functionality of the existing routine or program. It is generally provided in response to an unforeseen need or set of circumstances. Patching is also a common means of adding a new feature or function to a program until the next major version of the software is released.
Platform (IT)	A platform consists of an operating system, the computer system's coordinating program, which in turn is built on the instruction set for a processor or microprocessor, and the hardware that performs logical operations and manages data movement in the computer.
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.
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.
Receivables or debtors (in financial statements)	Money owed to the auditee by companies, organisations or persons who have procured goods and services from the auditee.
Vulnerability (IT)	In information security, a weakness or flaw (in location, physical layout, organisation, management, procedures, personnel, hardware or software) that may be exploited by an attacker to cause an adverse impact.

17.3 Acronyms and abbreviations used in this report

Acsa	*Airports Company South Africa*
AGSA	*Auditor-General of South Africa*
Apac	*Association of Public Accounts Committees*
Armscor	*Armaments Corporation of South Africa*
bn	*billion*
DEP	*department*
DPME	*Department of Planning, Monitoring and Evaluation*
DPSA	*Department of Public Service and Administration*
EC	*Eastern Cape*
ENE	*estimates of national expenditure*
FS	*Free State*
GP	*Gauteng*
HR	*human resource*
IFMS	*integrated financial management system*
IJS	*integrated justice system*
IT	*information technology*
KZN	*KwaZulu-Natal*
Land Bank	*Land and Agricultural Development Bank of South Africa*
LP	*Limpopo*
m	*million*
MP	*Mpumalanga*
MTSF	*Medium-term Strategic Framework*

NC	*Northern Cape*
NDP	*National Development Plan*
Necsa	*South African Nuclear Energy Corporation*
NW	*North West*
PE	*public entity*
Petroleum Agency SA	*SA Agency for Promotion of Petroleum Exploration and Exploitation*
PetroSA	*Petroleum Oil and Gas Corporation*
PFMA	*Public Finance Management Act*
Prasa	*Passenger Rail Agency of South Africa*
SAA	*South African Airways*
SABC	*South African Broadcasting Corporation*
Safcol	*South African Forest Company*
Sapo	*South African Post Office*
SCM	*supply chain management*
Scopa	*Standing Committee on Public Accounts*
Sita	*State Information Technology Agency*
SOE	*state-owned enterprise*
TVET	*technical and vocational education and training*
WC	*Western Cape*

NOTES

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