



AUDITOR - GENERAL

SECTION 4: REVIEW OF NATIONAL PUBLIC ENTITIES

4.1 Classification of public entities

Public entities are classified into different schedules based on their nature and level of autonomy. A brief review is provided below.

4.1.1 Schedule 2

Schedule 2 entities are referred to as the major public entities and are intended to generate profits and declare dividends. These entities have the most autonomy of all the public entities, as they operate in a competitive marketplace and are run in accordance with general business principles. In terms of section 66(3)(a) of the PFMA, schedule 2 public entities may also borrow money through the accounting authority of that entity, which implies that they also have extensive borrowing powers.

4.1.2 Schedules 3B and 3D

Schedule 3B and 3D entities are referred to as government business enterprises. These entities generate income, but may be either substantially self-funded or substantially government funded. As a result they have less autonomy than the schedule 2 public entities even though they are still run in accordance with general business principles. These entities also have limited borrowing powers.

4.1.3 Schedules 3A and 3C

The remaining public entities are classified as schedule 3A and 3C entities. These entities are normally extensions of a department with the mandate to fulfil a specific economic or social responsibility of government. They rely on government funding and public money, either by means of a transfer from the Revenue Fund or through statutory money. As such, these entities have the least autonomy.

The public entities reviewed for the purpose of this report only include the following schedules and are hereinafter referred to as national public entities:

- Schedule 2
- Schedule 3A
- Schedule 3B

Schedules 3C and 3D are provincial public entities and provincial business enterprises respectively.

4.2 Availability of information

4.2.1 Availability of information to the Auditor-General

In terms of section 55(1)(d) of the PFMA, the accounting authority for a public entity must submit within five months of the end of a financial year to the relevant treasury, to the executive authority responsible for that public entity and, if the Auditor-General did not perform the audit of the financial statements, to the Auditor-General –



A U D I T O R - G E N E R A L

- (i) an annual report on the activities of that public entity during that financial year;
- (ii) the financial statements for that financial year after the statements have been audited; and
- (iii) the report of the auditors on those statements.

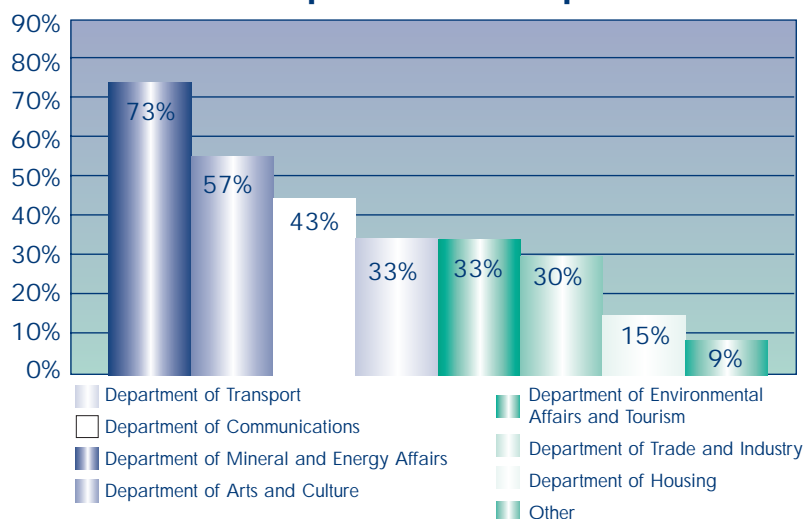
In total there are 191 (2002-03: 198) national public entities, of which 117 (2002-03: 110) were audited by my office. As at the end of August 2004 information on only 151 (2002-03: 136) of these entities was available, which represent 79% (2002-03: 69%) of all the national public entities. Forty entities (2002-03: 62), representing 21% (2002-03: 31%) of the total national public entities, either did not submit the relevant information to my office, or had not finalised their information at that date.

Table 11 and figure 16 provide a breakdown of the forty public entities for which information was not available, as well as the ministerial portfolio from which they originate.

Table 11. Entity information not submitted to the Auditor-General per ministerial portfolio

Ministerial portfolio	Total number of public entities per ministerial portfolio	Entities that did not submit information on time	Percentage of non-submission per portfolio
Transport	11	8	73%
Environmental Affairs and Tourism	7	4	57%
Communications	7	3	43%
Trade and Industry	18	6	33%
Minerals and Energy	9	3	33%
Housing	10	3	30%
Arts and Culture	27	4	15%
Other	102	9	9%
Total	191	40	21%

Figure 16. Percentage of information not submitted to the Auditor-General per ministerial portfolio





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The ministerial portfolios that submitted annual reports (or at least financial statements) for less than 30% of their public entities are as follows:

- Transport
- Environmental Affairs and Tourism
- Communications
- Trade and Industry
- Minerals and Energy

The above portfolios represent 60% (24 entities out of 40) of the total entities that did not submit information to my office.

The analysis I am able to provide in the general report is therefore limited to 151 entities, which makes it incomplete and also limits comparability between financial years. Although there has been an improvement on the 2002-03 financial year, this contravention of the PFMA is an obstacle to the accountability process and a matter of grave concern.

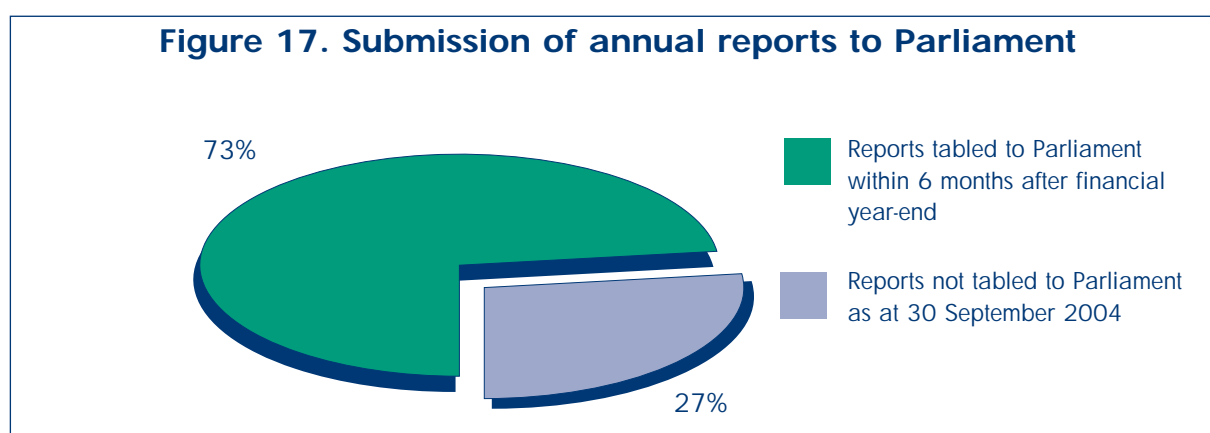
The National Treasury published a list of listed public entities on 1 June 2004 and this list was reconciled with the list of public entities that I have audited. The following entities were noted as being absent from the National Treasury list, which were however audited by my office:

- Foundation for Education, Science and Technology – Pretoria
- SA Housing Fund

The updating of the list of listed public entities also remains a practical problem and could have a significant impact on public accountability.

4.2.2 Availability of information to Parliament

Section 65 of the PFMA requires the executive authority to table the annual report, financial statements and audit report in Parliament within six months after year-end. Of the 191 public entities 165 have 31 March as their year-end and these 165 entities need to table their reports by 30 September 2004. On 30 September 2004, 73% (121 public entities) had tabled their annual report, financial statements and audit report to Parliament, with 27% (44 public entities) not tabled per PFMA requirements. Figure 17 below sets out the above detail.





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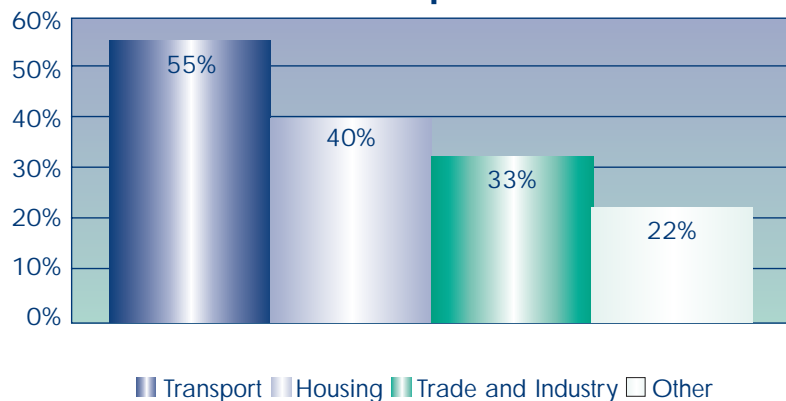
For the 27% (44 public entities) of outstanding reports to Parliament, table 12 below details the three ministerial portfolios which had the highest percentage of reports on public entities not tabled in Parliament by 30 September 2004 per ministerial portfolio:

Table 12. Ministerial portfolios: Reports on public entities not tabled in Parliament

Ministerial portfolio	Total number of entities per portfolio	Number of public entities not tabled in Parliament	Percentage public entities not tabling per portfolio
Transport	11	6*	55%
Housing	10	4	40%
Trade and Industry	18	6	33%
Other	126	28	22%
Total	165	44	27%

* Two entities tabled annual reports, but did not submit copies to my office.

Figure 18. Percentage of public entities not tabled in Parliament, per ministerial portfolio



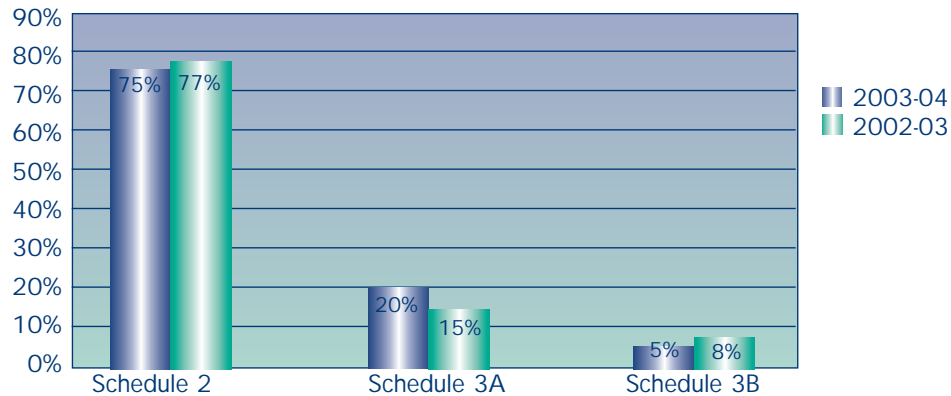
4.3 Analysis of revenue for the different scheduled public entities

For the 151 entities included in the analysis the total revenue was just over R145 billion (2002-03: R125 billion). Revenue received by the South African Revenue Service of R315 billion (2002-03: R294 billion) has been excluded since it represents taxes levied by government and collected by SARS on behalf of government on an agency basis. Total revenue of the remaining entities consists of government grants, investment income and other income. Other income encompasses sales of products and services and revenue received or imposed by legislation. Figure 19 below, which provides a breakdown of the percentage of own income generated per PFMA schedule, indicates that this has not changed materially from the prior financial period.



AUDITOR - GENERAL

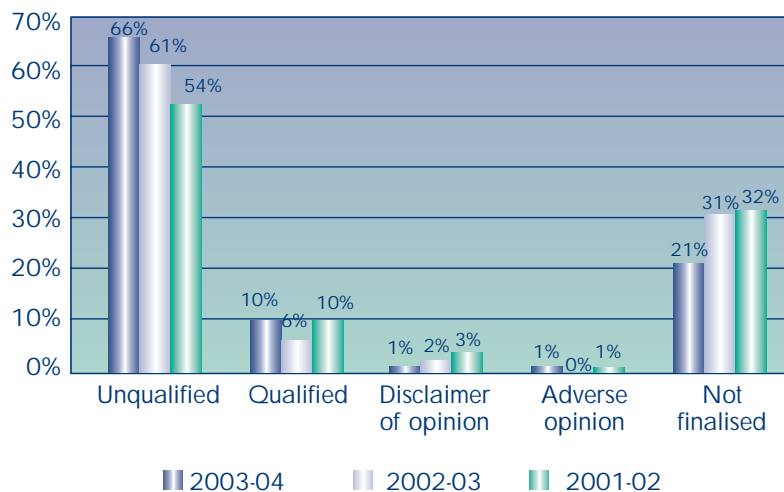
Figure 19. Breakdown of own income generated by national public entities



4.4 Audit opinions

The audit opinions on the 151 public entities, for which information was received and analysed, show that there is a decrease in the percentage of entities that received a qualified audit opinion (adverse, disclaimer or "except for"). Refer to figure 20 for more details.

Figure 20. Public entity audit opinions



The unqualified audit opinions have increased year-on-year from 54% (2002) to 66% (2004), representing an improvement of 12% over that period. However, the fact that 21% (2002-03: 31%) of the required information is outstanding, makes it difficult to assess the overall picture.

It was noted that 12 public entities, detailed in table 13 below, were identified as having received qualified audit opinions for the last three years. Of the twelve entities, six entities relate to the Department of Arts and Culture.



A U D I T O R - G E N E R A L

Table 13. Details of public entities that received qualified audit opinions for the past three financial years

No.	Public entity	Ministerial portfolio	PFMA schedule	2003-04 audit opinion	2002-03 audit opinion	2001-02 audit opinion
1	Ingonyama Trust Board	Agriculture and Land Affairs	3A	Disclaimer of opinion	Disclaimer of opinion	Disclaimer of opinion
2	Ncera Farms (Pty) Ltd	Agriculture and Land Affairs	3B	Qualified	Qualified	Qualified
3	Voortrekker Museum Pietermaritzburg	Arts and Culture	3A	Adverse opinion	Qualified	Disclaimer of opinion
4	SA Blind Workers Organisation, Johannesburg	Arts and Culture	3A	Qualified	Qualified	Qualified
5	State Theatre, Pretoria	Arts and Culture	3A	Qualified	Qualified	Qualified
6	The Playhouse Company, Durban	Arts and Culture	3A	Qualified	Qualified	Qualified
7	Market Theatre Foundation	Arts and Culture	3A	Qualified	Qualified	Qualified
8	The Renaissance Theatre t/a The Spoornet State Theatre	Arts and Culture	3A	Qualified	Qualified	Qualified
9	Castle Control Board	Defence	3A	Qualified	Qualified	Qualified
10	Unemployment Insurance Fund	Labour	3A	Disclaimer of opinion	Disclaimer of opinion	Disclaimer of opinion
11	Mine Health & Safety Council	Minerals and Energy	3A	Qualified	Disclaimer of opinion	Disclaimer of opinion
12	Cross-border Road Transport Agency	Transport	3A	Qualified	Disclaimer of opinion	Disclaimer of opinion

Of the qualification issues raised, it appears that the majority could be attributed to level 2: policy framework issues. This implies that the accounting authority had not yet put in place mechanisms to facilitate effective internal controls.

The remainder of the issues could be attributed to the "adequacy" of internal controls or training and capacity issues.

4.5 Matters emphasised

Although the percentage of entities for which information was not available decreased to 21% from the previous year's 31%, the average number of reports that contained an emphasis of matter paragraph

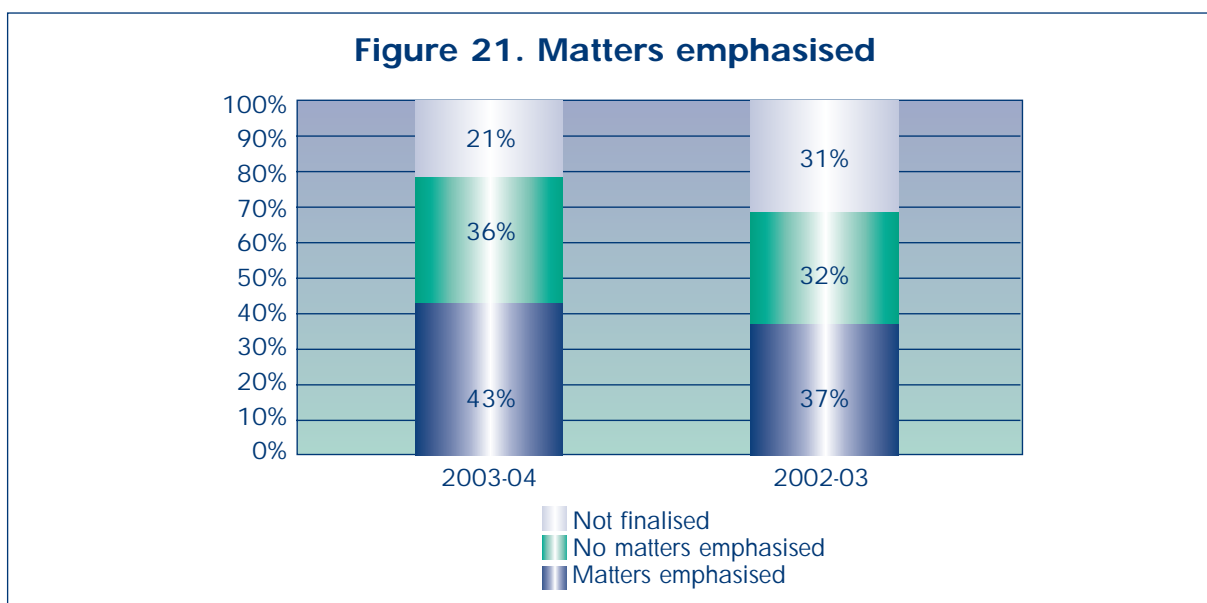


A U D I T O R - G E N E R A L

increased from 37% to 43%. It is thus anticipated that of the outstanding reports, a significant number will also feature emphasis of matter paragraphs.

Of those entities audited by my office, 189 issues were assessed in terms of the financial management capability model. Of these issues the majority were classified as level 2: policy framework issues and therefore represent areas where the accounting authority has not put in place a policy framework. The remainder were issues regarding the "adequacy" of internal controls or training and capacity.

These findings indicate that the state of maturity in the area of financial management of public entities is similar to that of the national departments.



There does, however, appear to be a tendency for more matters to be emphasised when my office conducts audits.

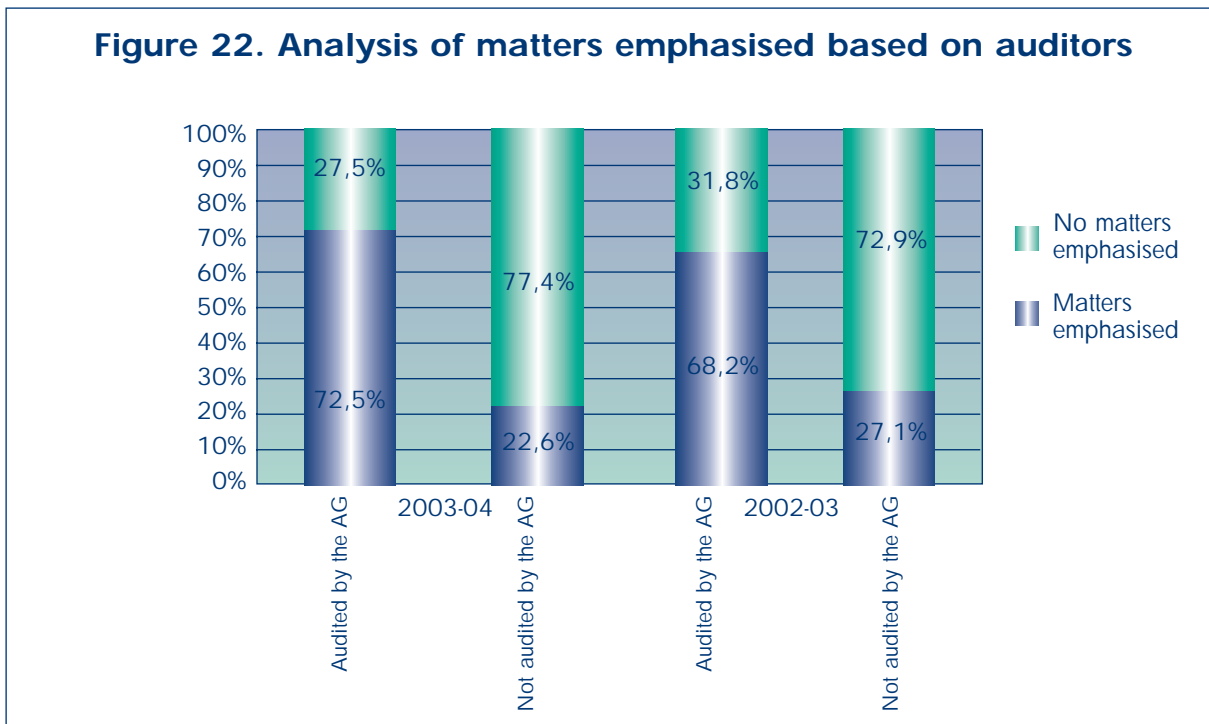
In 72,5% (2002-03: 68,2%) of the audit reports issued by my office, one (or more) matter was emphasised in the report. In cases where the audit was performed by an external audit firm, appointed in terms of section 58(1)(b) of the PFMA, only 22,6% (2002-03: 27,1%) of the reports contained an emphasis of matter paragraph.

This might indicate that auditors appointed in terms of section 58(1)(b) of the PFMA do not place sufficient emphasis on the importance of reporting legislative and internal control requirements such as:

- Non-compliance with laws and regulations, e.g. the PFMA and Treasury Regulations, including the basic elements of a policy framework (45% of matters emphasised by my office included these issues)
- Internal audit and audit committees (9,5% of matters emphasised by my office included these issues)
- Asset management (12% of matters emphasised by my office included these issues)



A U D I T O R - G E N E R A L



4.6 Compliance issues

Whilst reviewing the national public entities, a number of requirements to which public entities are subject and that appear to be problematic to the entities were identified. They are listed below with a brief explanation of the issue.

- Performance information: No guidance exists on what to report and where to report.
- Irregular and fruitless and wasteful expenditure, material losses: No guidance exists on what to report and where to report (guidance in this regard does exist for departments as the National Treasury has prescribed the format for the annual report of departments).
- Directors’ and executive members’ emoluments: These definitions have not been clearly defined and it is disclosed inconsistently.
- Materiality and significance framework: No guidance exists on what to report.

It is the responsibility of the National Treasury to provide direction and guidance. The National Treasury does require certain information to be reported, but does not provide guidance on the exact disclosure requirements.

Where appropriate, the issues are discussed below to provide further background information.

4.7 Performance information

Section 55(2)(a) of the PFMA states that "the annual report and financial statements...must-

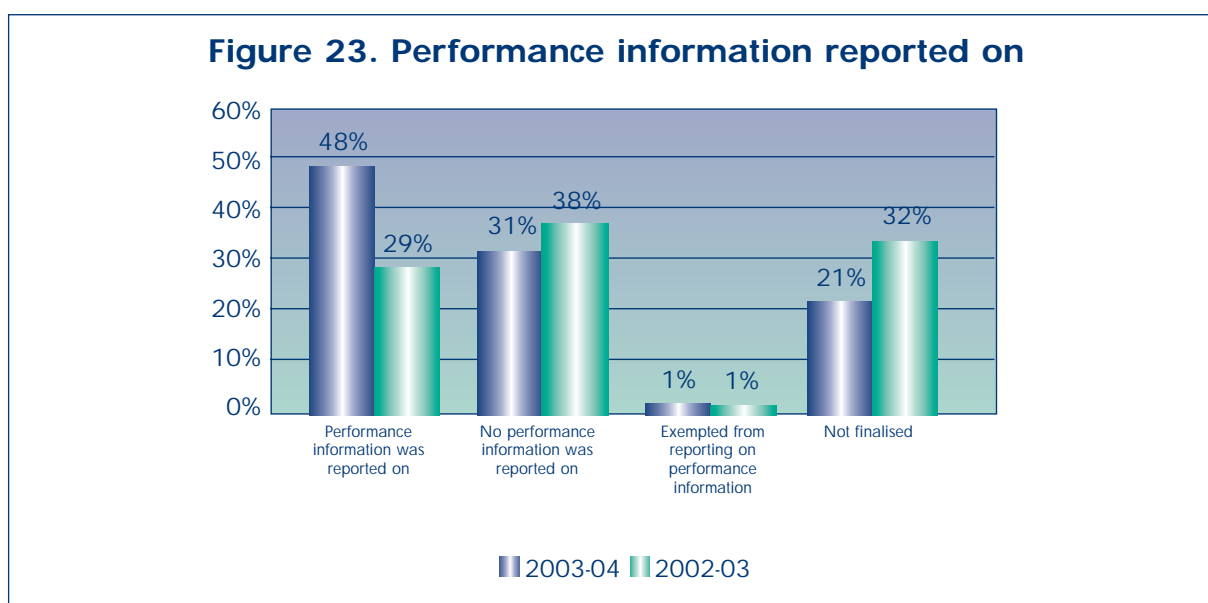
- (a) fairly present the state of affairs of the public entity, its business, its financial results, its performance against predetermined objectives and its financial position as at the end of the financial year..."



A U D I T O R - G E N E R A L

The requirement in terms of performance against predetermined objectives represents a fundamental and important characteristic of the PFMA, namely that entities are not expected to provide information merely on their financial health and performance, but also on aspects such as service delivery. This broader information is a crucial element of the overall accountability process. In particular, it provides an important bridge between the expectations of the stakeholders of audit and annual reports and the information that is currently provided. There has been an increase of 19% in respect of entities that reported on performance information, but it should be reiterated that the criteria for judging what constitutes performance information were subjective, as no guidance has been provided by the National Treasury.

Performance information reported on for the public entities analysed is set out in figure 23 below.



4.8 Irregular and fruitless and wasteful expenditure and material losses

In total, the following were reported as irregular and fruitless and wasteful expenditure and material losses in the financial statements of the public entities:

Table 14. Irregular and fruitless and wasteful expenditure and material losses

Type	Amount (R)	Number of entities
Irregular expenditure	9 340 678	9
Fruitless and wasteful expenditure	423 123	12
Material losses	939 000	7

In the context of the annual financial statements, the reporting of irregular and fruitless and wasteful expenditure was minimal. This is with the exception of the South African Weather Service (R6,9 million) and the Film and Publication Board (R1,5 million), who reported irregular expenditure since they had entered into finance lease agreements without the consent of the minister.



A U D I T O R - G E N E R A L

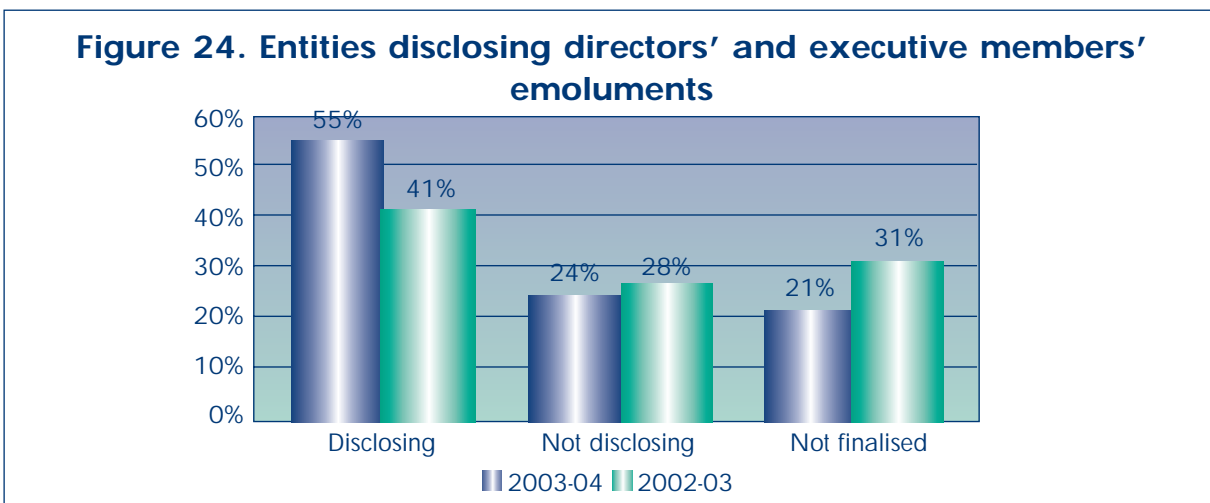
4.9 Directors’ and executive members’ emoluments

The disclosure of directors’ and executive members’ emoluments in the annual financial statements is required in terms of Treasury Regulation 28.1.1. Despite this requirement, 24% (46) of the entities did not disclose the information. In addition, there was also a lack of consistency with respect to the classification of directors and executive members, as well as the level to which the disclosure was made.

The lack of consistency in the reporting of the directors’ and executive members’ emoluments is an area of concern as it prevented me from establishing the average salary per director and executive member.

An alarming fact identified during my analysis was the seemingly exorbitant fees and bonuses paid to directors and executive members. Due to the inconsistent disclosure of directors’ and executive members’ remuneration, I will refrain from disclosing specific entities and names. This is, however, a matter that will be investigated further and my future reports may include more detail in this regard.

One entity that should be mentioned is the Ikangala Water Board. The board received a transfer payment from the Revenue Fund of R2 million. The only other income received related to interest of R63 000, however, the total directors’ remuneration for the year was R2,714 million. The directors’ remuneration exceeded the transfer payment and interest received. This resulted in a net loss for the year amounting to R1,297 million. Although this may seem to be insignificant, it is of concern to me, given the objective of the PFMA, namely "to maximise delivery through the efficient and effective use of limited resources".



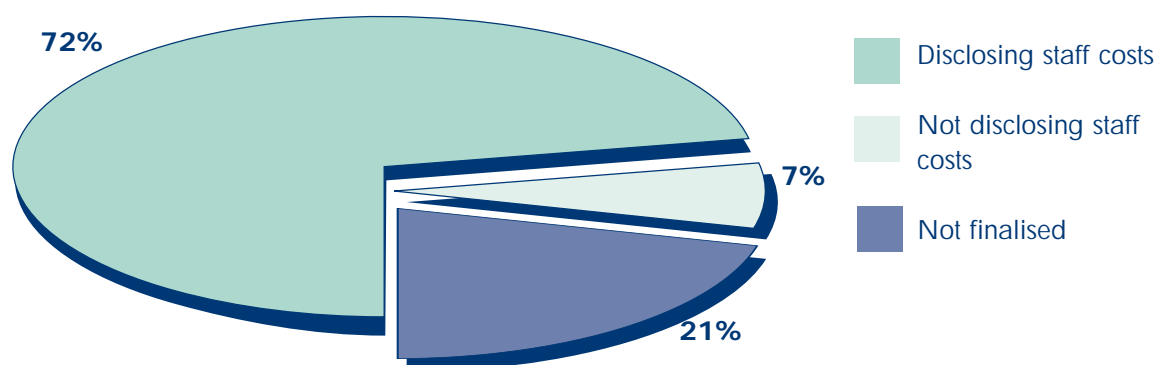
4.10 Staff costs

Staff costs for the public entities that were analysed are set out in figure 25 below. Public entities should prepare annual financial statements in terms of Statements of Generally Accepted Accounting Practice (GAAP). Paragraphs 81 and 84 of Accounting Standard AC 101 require the disclosure of staff costs. Seven per cent of the public entities did not disclose their staff costs.



AUDITOR - G E N E R A L

Figure 25. Staff costs disclosure (excluding directors' and executive members' emoluments)



4.11 Public entities' financial performance

One of the fundamental principles of GAAP is comparability of financial statements of an entity over a period of time to identify trends in its financial position and performance. In the private sector, financial ratios have been developed to determine if the financial position of the entity is healthy, but in the public sector no generally accepted ratios have been developed.

To compare the public entities, various analyses per schedule were performed to highlight current financial ratios, for example:

- Average revenue generated per PFMA schedule
- Average expenditure analysis per PFMA schedule
- Average income statement analysis per PFMA schedule
- Comparison of total average assets
- Analysis of non-current to current assets
- Current ratio analysis
- Net profit/(loss) analysis (2002-03 vs 2003-04)

In Figure 26 below, total revenue per entity is grouped into three categories, namely average other revenue, average investment income and average transfer payment. What is of significance in this analysis is that the average transfer payment received per entity is rather immaterial in relation to the total revenue it generated. Schedule 3A entities received the highest average transfer payment of 26% of their total income.



A U D I T O R - G E N E R A L

Figure 26. Revenue generation per PFMA schedule

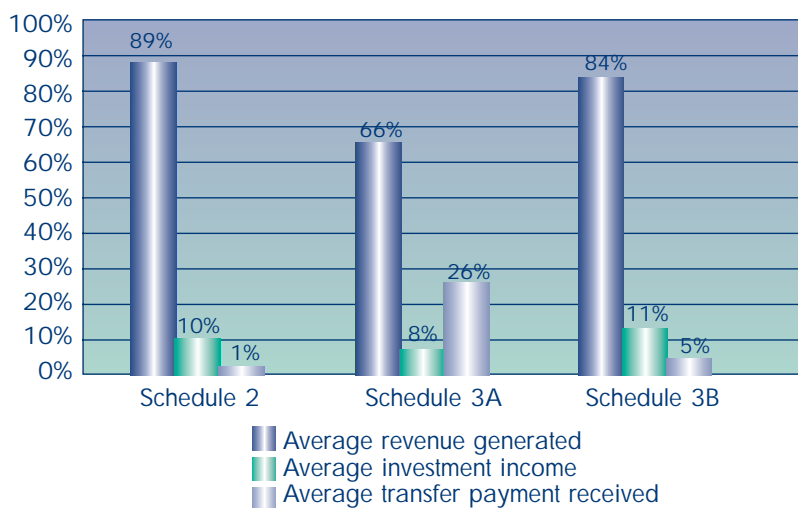
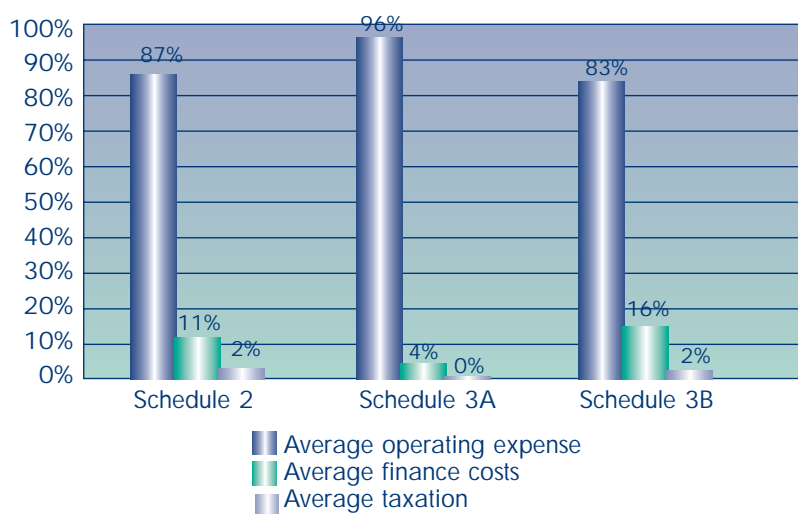


Figure 27 provides details relating to the average operating expense before finance costs and taxation, the average finance costs and the average taxation. On average, finance costs constituted 11% (schedule 2), 4% (schedule 3A) and 16% (schedule 3B) of total expenditure respectively. In comparison, investment income constituted 10% (schedule 2), 8% (schedule 3A) and 11% (schedule 3B) of total revenue generated.

Figure 27. Expenditure analysis per PFMA schedule

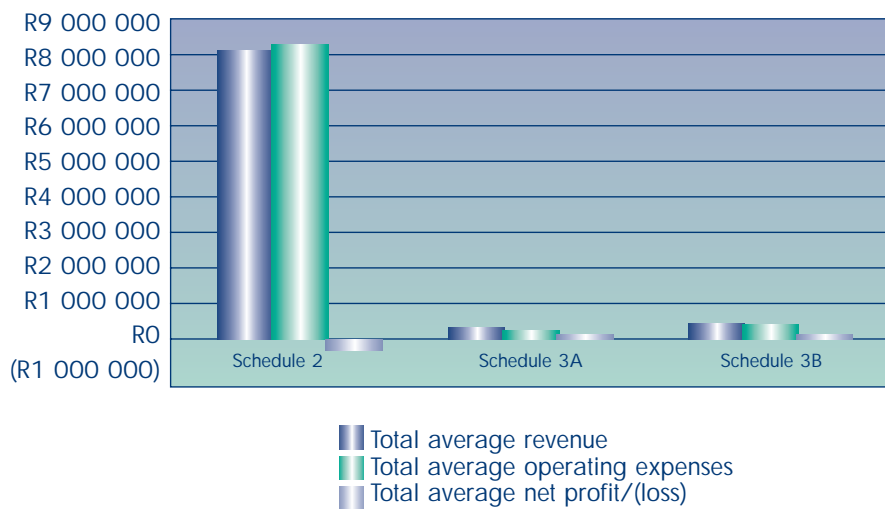


Based on the above analysis and as reflected in figure 28 below, the entities have not generated significant profits during the current period.



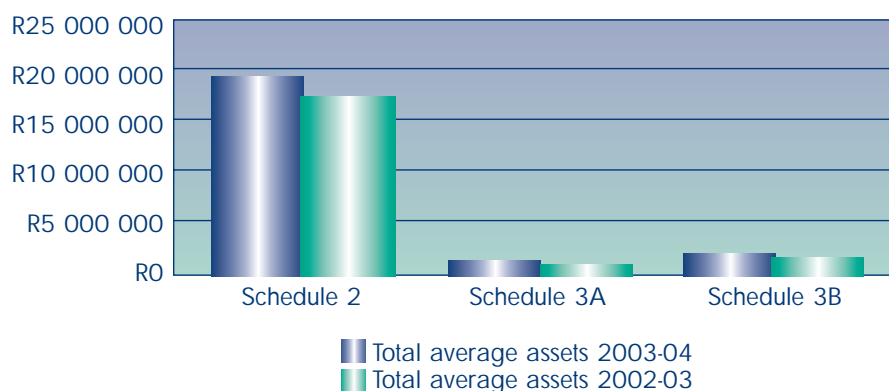
AUDITOR - GENERAL

Figure 28. Average income statement analysis per PFMA schedule (R'000)



Total assets year-on-year remained fairly consistent, except for schedule 2 entities. Significant investments in assets were made by Eskom and Transnet during the current financial period, which increased the total average for schedule 2 entities. Further analysis (in figure 30) indicates that this increase in the value of total assets is due to significant increase in the comparative value of non-current assets for the schedule 2 entities, as a result of large capital investments.

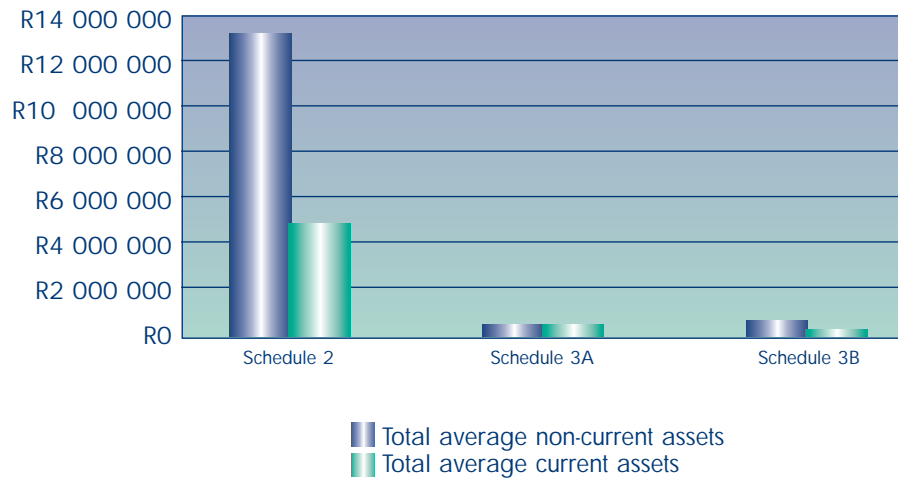
Figure 29. Comparative value of total average assets year-on-year (R'000)





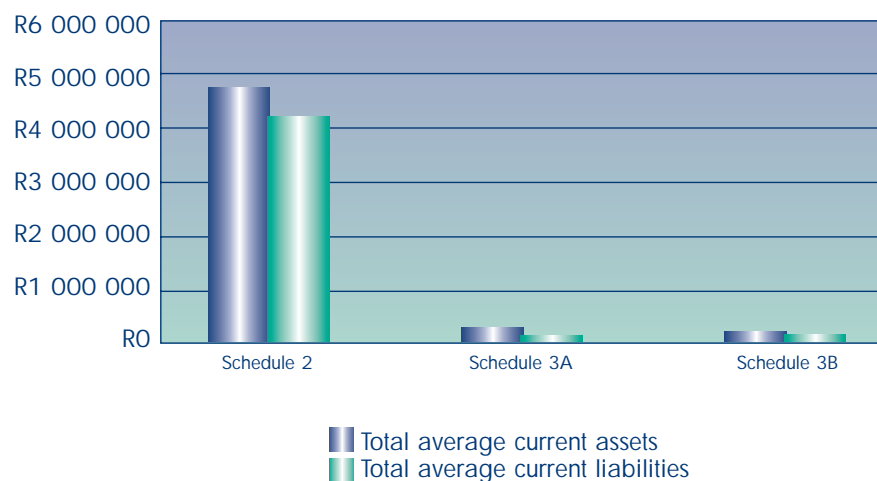
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Figure 30. Comparative value of non-current assets to current assets per PFMA schedule (R'000)



The current ratio analysis illustrates that the entities are primarily liquid and would be able to meet their debt requirements as and when they become due.

Figure 31. Current ratio analysis per PFMA schedule (R'000)



The significant movement in the net profit / (loss) of the schedule 2 entities has been attributed to the increased loss incurred by Transnet during the current period. The losses of approximately R6,3 billion (2002-03: R421 million) have resulted in a skewed analysis year-on-year. A large portion of these losses have been attributed to the SAA derivative hedge book, as reported widely in the press.



AUDITOR - GENERAL

Figure 32. Net profit/(loss) analysis per PFMA schedule (R'000)