



AUDITOR - GENERAL

Table 5. Details on 16 public entities receiving a qualified audit opinion for 2002-03

No	Public entity	Ministerial portfolio	PFMA schedule	2002-03 audit opinion	2001-02 audit opinion
1	Ingonyama Trust Board	Agriculture and Land Affairs	3A	Disclaimer of opinion	Disclaimer of opinion
2	Mines and Works Compensation Fund	Health	3A	Disclaimer of opinion	Unqualified
3	Unemployment Insurance Fund	Labour	3A	Disclaimer of opinion	Disclaimer of opinion
4	Mine Health & Safety Council	Minerals and Energy	3A	Disclaimer of opinion	Disclaimer of opinion
5	Ncera Farms (Pty) Ltd	Agriculture and Land Affairs	3B	Qualified	Qualified
6	Iziko Museums of Cape Town	Arts and Culture	3A	Qualified	Qualified
7	Natal Museum, Pietermaritzburg	Arts and Culture	3A	Qualified	Qualified
8	Northern Flagship Institute, Pretoria	Arts and Culture	3A	Qualified	Disclaimer of opinion
9	Performing Arts Council of Free State	Arts and Culture	3A	Qualified	Unqualified
10	SA Blind Workers Organisation, Johannesburg	Arts and Culture	3A	Qualified	Qualified
11	State Theatre, Pretoria	Arts and Culture	3A	Qualified	Qualified
12	The Play House Company, Durban	Arts and Culture	3A	Qualified	Qualified
13	Voortrekker Museum, Pietermaritzburg	Arts and Culture	3A	Qualified	Disclaimer of opinion
14	Police, Private Security, Legal and Correctional Services Training Authority (POSLEC SETA)	Labour	3A	Qualified	Unqualified
15	Secondary Agricultural Sector Education and Training Authority (SETASA)	Labour	3A	Qualified	Unqualified
16	Africa Institute of South Africa, Pretoria	Science and Technology	3A	Qualified	Unqualified

Of the entities previously qualified the most significant improvement was in terms of the South African Diamond Board, that received an adverse audit opinion for 2001-02 and an unqualified audit opinion for 2002-03.



AUDITOR - GENERAL

Table 6. Disclaimers of audit opinions

Entity	Portfolio	Reason for the disclaimer of audit opinion	Opinion in 2001-02	Issue raised in 2002 (Yes:✓ No:x)
Inqonyama Trust Board	Agriculture and Land Affairs	<p>Inadequate debtors system</p> <p>The serious problems in the system of internal controls to maintain and record debtors indicated a lack of effective and efficient management policy and control which did not contribute to a sound financial environment. The following problems placed a severe limitation on the audit scope:</p> <ul style="list-style-type: none"> - The current debtors system did not provide sufficient information regarding the debtors in arrears, debtors paid in advance or the roll forward of debtor balances from the previous financial years. - The 2001-02 royalty debtors amount was written off out of income collected during the 2002-03 financial year, even though not all the debtors had paid, thereby understating the debtors and royalty income figures in the financial statements. - Debtors were not raised for trading permission to occupy, therefore the balances were understated <p>Arrear rates – eThekweni Municipality and other municipalities</p> <p>The potential liability for rates due to municipalities for land owned within the board's demarcated areas was not disclosed in the financial statements. The accumulated amount in the region of R88,4 million was already due to the eThekweni Municipality in respect of rates in arrear and it is questionable whether the trust would be able to continue as a going concern in the light of this potential liability as it could lead to immediate insolvency. As there is a dispute over the amounts, ministerial intervention needs to take place to resolve this long outstanding matter on which no visible progress is being made.</p>	Disclaimer	✓
		<p>Accounts payable</p> <p>No income collected from royalties and permission to occupy had been paid over to the various tribal authorities, as required by the KwaZulu-Natal Ingonyama Trust Act, 1994 (Act No. 3KZ of 1994) for the past number of years, and no amount was shown as owing to the tribal authorities under the accounts payable. From discussions, the amount owing is substantial, being in the region of R22,0 million.</p>		x



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

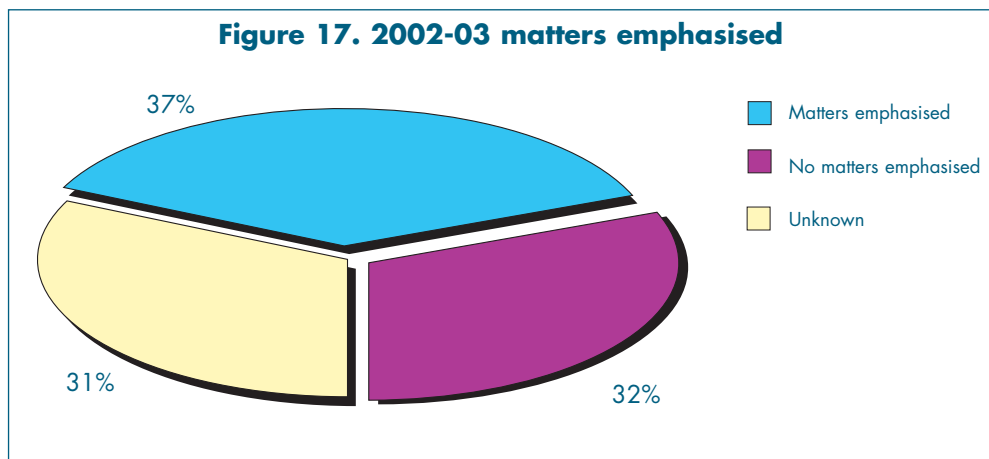
Entity	Portfolio	Reason for the disclaimer of audit opinion	Opinion in 2001-02	Issue raised in 2002 (Yes:✓ No:✗)
Unemployment Insurance Fund (UIF)	Labour	With regard to the statistical framework and data collection, the fund did not know the exact number and characteristics of its insured persons, nor did it know the exact entitlements that these persons had accrued.	Disclaimer	✓
		The fund experienced a material breakdown in internal control systems and procedures with regard to:		✓
		Contributions receivable – arrear contributions were not followed up, individual accounts were not monitored, queries of employers were not followed up.		✓
		Benefits payable – unreconcilable differences existed between the subsystem and the general ledger.		✓
		Administration of bank accounts and the updating of accounting records resulted in unreconciled balances.		✓
		Deficiencies in contributions by employers and employees with regard to the following: - collection of arrear contributions, - the penalty programme of charging and collecting penalties and interest for late receipt was not effectively applied, - the controls to ensure the accuracy, completeness and validity of declarations of earnings by employers did not function effectively during the period.		✓
		Personnel, administration and rental expenses of R309,2 million relating to services rendered by the Department of Labour could not be audited as they were not based on a scientific time study but rather on approximations.		✓
		The fund did not provide for accrued leave and post-retirement benefits.		✓
		There were significant weaknesses in the general control environment of the fund with regard to programme change controls, security administration and monitoring and logical access security.		✗
		The existence of the majority of movable fixed assets could not be verified as a result of an incomplete and inaccurate fixed asset register.		✗
Mine Health and Safety Council	Minerals and Energy	Inability to verify the accuracy, validity and completeness of the accounting records relating to accounts receivable, levy income, staff costs and VAT liability due to inadequate control and accounting systems in place during the year under review.	Disclaimer	
		The provision made for post-retirement medical benefits was based on the valuation of the liability on 1 September 2003 and not on 31 March 2002.		
Mines and Works Compensation Fund	Health	The auditors were not able to verify the interest on investments of the fund.	Emphasis of matter	✗



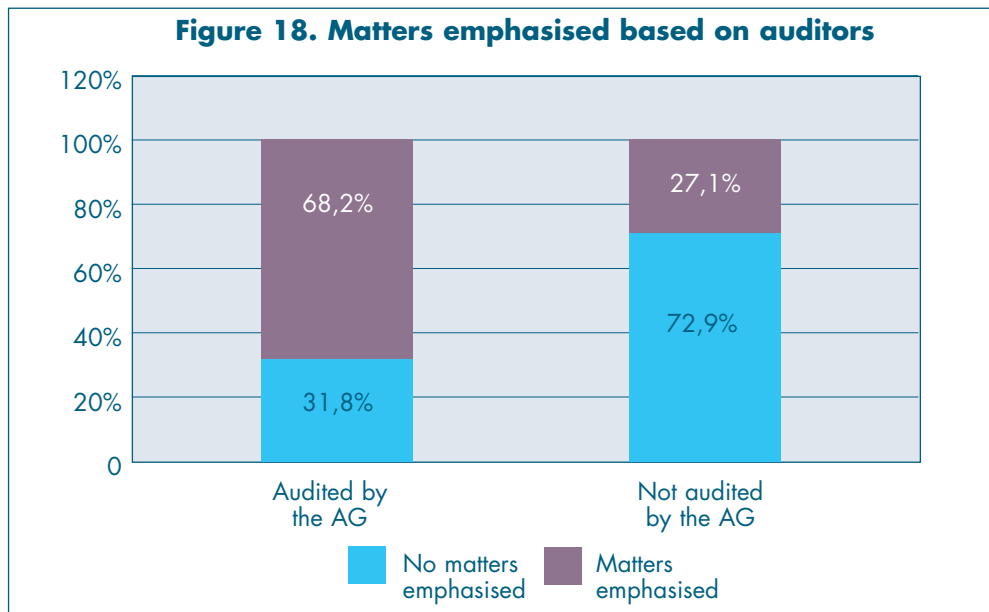
A U D I T O R - G E N E R A L

3.5 MATTERS EMPHASISED

In terms of matters emphasised there is once again a tendency towards fewer matters being reported than in the previous year. However, once again the situation applies only to those entities that submitted information and therefore 31% still remains unknown, as depicted in figure 17 below.



There does, however, appear to be a tendency for more matters to be emphasised when audits are conducted by my office. Figure 18 below demonstrates that the likelihood of a matter being emphasised by my office is almost 70%, whereas for public entities not audited by my office, the incidence is under 30%. This might indicate that the external auditors do not give sufficient attention to the requirements specific to government, for example the requirements of the PFMA and the associated Treasury Regulations.





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

3.6 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 terms have not been defined.
- 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 general information to be reported but does not provide guidance on the exact nature of the information to be reported or where in the annual report the information should be disclosed.

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

3.7 PERFORMANCE INFORMATION

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

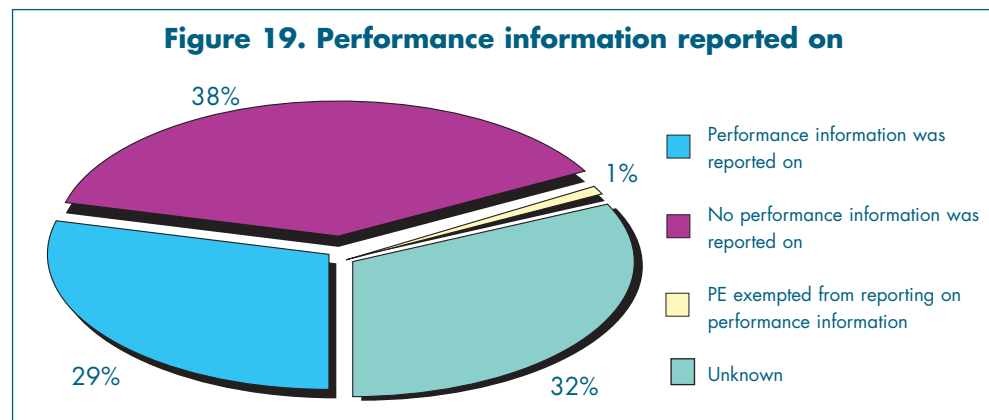
Fairly present the state of affairs of the public entity, its business, its financial results, its performance against predetermined objectives and its financial position at the year-end..." (own emphasis)

The requirement in terms of performance against predetermined objectives represents a fundamental and important characteristic of the PFMA, namely that entities are not expected merely to provide information 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. A disappointing number of entities actually provided clear performance information in their reports.



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

Figure 19 below demonstrates the current under-reporting of performance information. Only 29% of cases could clearly be viewed as providing performance information. 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.



3.8 IRREGULAR AND FRUITLESS AND WASTEFUL EXPENDITURE, MATERIAL LOSSES

The reporting of irregular and fruitless and wasteful expenditure was minimal. This is with the exception of Eskom, who reported the following:

- wasteful and fruitless expenditure in terms of excess foreign exchange cover of R128 million; and
- material losses of conductor theft of R77 million.

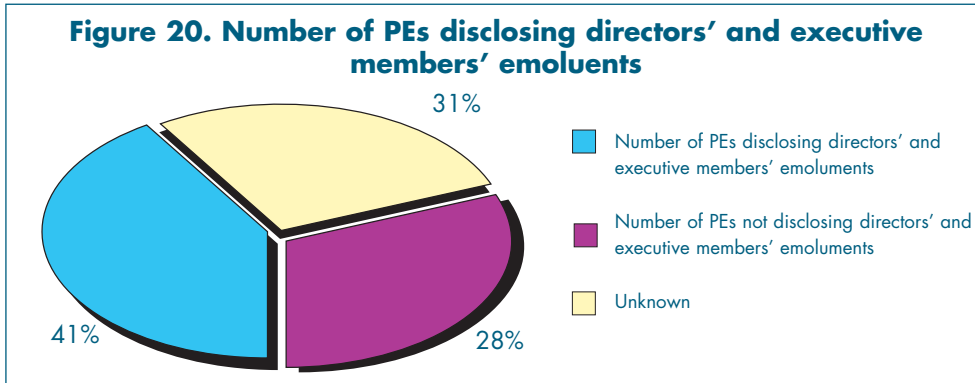
The total remaining reported fruitless and wasteful expenditure was R3,7 million. The total remaining reported material losses was a mere R0,2 million. The cases of irregular expenditure were nil. This implies that there may be an understatement of these categories of expenditure. As stated earlier, this could in part be attributed to the lack of guidance issued by the National Treasury.

3.9 DIRECTORS' AND EXECUTIVE MEMBERS' EMOLUMENTS

The analysis of directors' and executive members' emoluments was once again limited by the availability of information. Of the 69% of public entities for which information was available, 28% of the entities (57) did not disclose any emoluments. Figure 20 below shows the overall position. The disclosure of directors' and executive members' emoluments in the annual report or financial statements was used for this analysis.



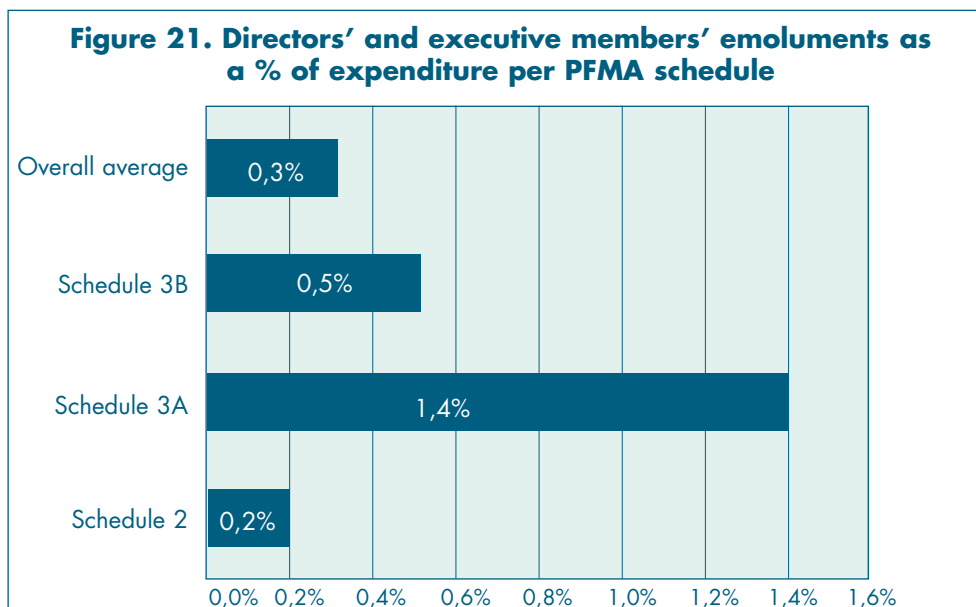
A U D I T O R - G E N E R A L



Of these 57 public entities, 19 public entities fell under Labour and 18 public entities fell under Arts and Culture. The two portfolios constituted 37 out of 57 (or 65%) of the entities failing to disclose directors' emoluments. Of the 19 public entities falling under Labour, 14 were State Education and Training Authorities.

Of the 57 public entities not disclosing directors' emoluments, 50 are schedule 3A public entities (representing 88%). Figure 21 below shows the marked differences between the different schedules of the entities that did report directors' emoluments, with schedule 3A public entities paying a much higher proportion of total expenditure before finance costs and taxation to directors and executive members.

The information provided below in figure 21 has limitations. It is only based on 41% of the national public entities. The concept of directors' and executive members' emoluments is not defined and is therefore subject to the individual interpretation of each entity.





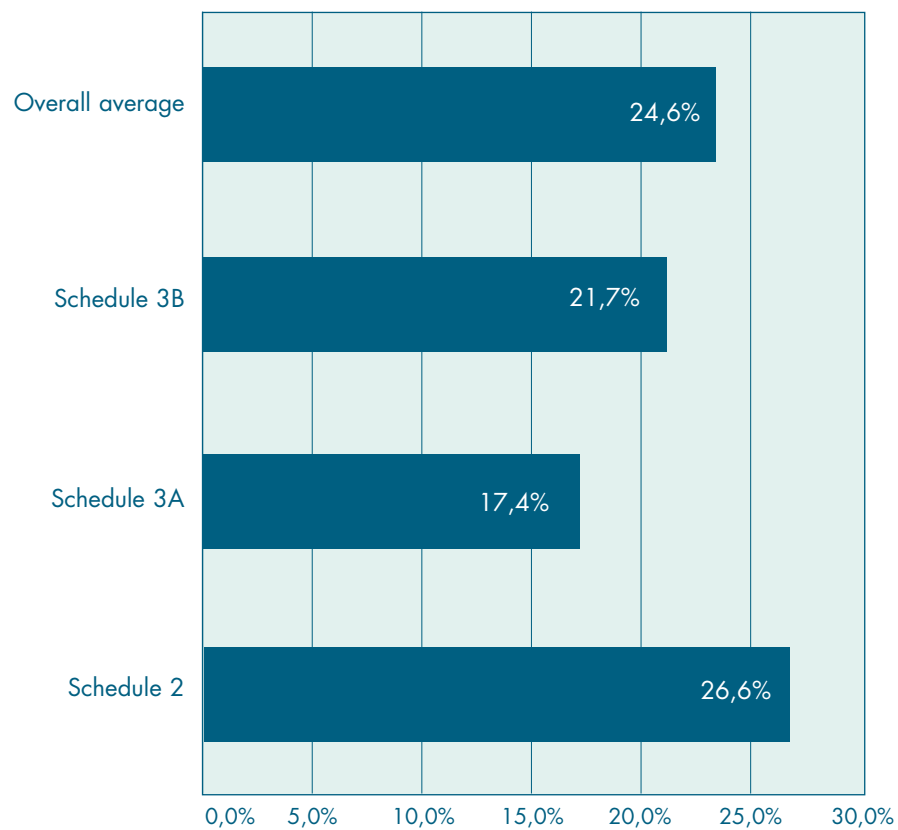
AUDITOR - GENERAL

From figure 21 above and the information provided on disclosure it appears that the schedule 3A public entities are the most reluctant to disclose directors' and executive members' emoluments. In addition, it could be deduced that the schedule 3A public entities are paying their directors and executive members considerably higher emoluments. One significant factor to be taken into consideration is the relative size of the different public entities. The average expenditure for schedule 2 entities is approximately R6362,4 million, for schedule 3A R163,6 million and schedule 3B R356,8 billion.

3.10 STAFF COSTS

Staff costs for the public entities that were analysed as set out in figure 22 provided a different picture to that of the directors' and executive members' emoluments. The schedule 2 entities had the highest ratio of staff costs as a percentage of their expenditure whereas they had the lowest ratio of directors' and executive members' emoluments as a percentage of their expenditure. In contrast the schedule 3A entities had the highest directors' and executive members' emoluments ratio and the lowest staff costs ratio.

Figure 22. Staff costs (excluding directors' and executive members' emoluments) as a % of expenditure per PFMA schedule





AUDITOR - GENERAL

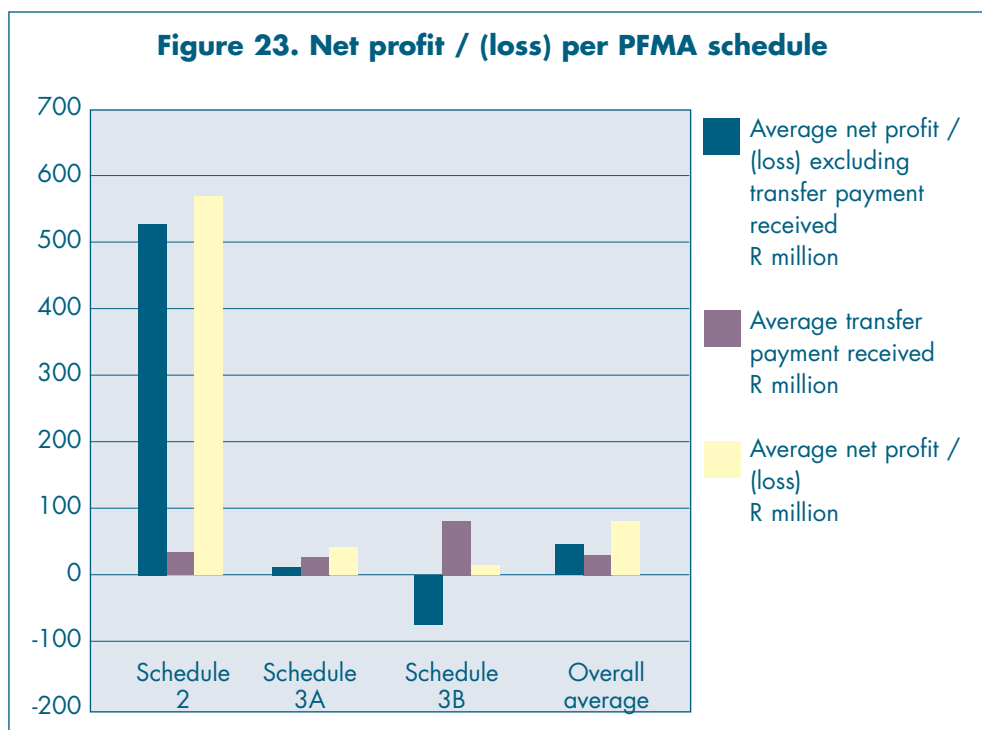
Although the difference in the scale of schedule 2 public entities may give rise to economies of scale that could explain the difference, there is still a difference between schedules 3A and 3B that shows the opposite situation to the proportion of directors' and executive members' emoluments.

3.12 PUBLIC ENTITIES' FINANCIAL PERFORMANCE

The analysis of the financial performance of national public entities examined the following financial information:

- Net profit/(loss)
- Return on assets
- Debt/Equity ratio

The net profit figure has once again shown an interesting distinction between the different schedules of public entities. The most interesting case is the schedule 3B entities (government business enterprises) that are in essence making losses that are subsidised by the transfer payments they receive. In addition, the schedule 3B entities have a poor return on asset ratio and a high level of debt to their equity. All these factors could point to financial problems for the business enterprises. However, business enterprises as defined in paragraph 3.1 may be substantially self funded or government funded even though they are still run in accordance with ordinary business principles.





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

The following table shows a summary of the ratios per schedule and further highlights the poor performance of the schedule 3B entities. In addition, the performance of the schedule 2 entities in terms of return on assets is only 4,6%.

Table 7. Overall financial performance per schedule

Schedule	No. of public entities reviewed	Average net profit/ (loss) excluding transfer payments received R million	Return on assets	Debt to equity ratio
Schedule 2	14	537,7	4,6%	32,3%
Schedule 3A	96	10,3	10,2%	4,5%
Schedule 3B	26	(71,2)	1,7%	30,0%
Average		49,0	4,9%	31,4%

The overall best and worst performers in terms of each of the ratios as shown in table 7 above are listed in annexure 3.3.

In terms of the debt to equity ratio a particularly interesting outcome is that the portfolios of Housing and Water Affairs and Forestry (for entities included in various schedules) have debt to equity ratios that are considerably higher than the average. The average as stated above is 31,4%; however, the Housing portfolio's average is 137,9% and Water Affairs and Forestry has an average of 77,6%.

4. AUDIT FLAVOURS

4.1 SPECIFIC ISSUES RELATING TO OTHER AUDITS

In recent years I have tried to focus on the key underlying problems that are giving rise to the reported audit findings. These audit flavours are:

- Asset management
- Control environment
- Procurement
- Human resources management
- Capacity

Each of the audit flavours is discussed below.