

## // SECTION 7

> >

*Governance, oversight and  
sustainability of state-owned entities*

## INTRODUCTION

Schedule 2 of the Public Finance Management Act lists 21 'major' public entities, commonly known as state-owned entities or SOEs. These SOEs are independent entities, partially or fully owned by the state, established to achieve the various socio-economic goals of government. They are expected to fulfil a dual commercial and developmental role, generate profits and declare dividends, and be run in accordance with general business principles.

**Government**, through the respective executive authorities (ministers), **represents the sole shareholder of these SOEs**. The shareholder is obligated to appoint an accounting authority, which also constitutes the board of directors in terms of the Companies Act. The accounting authority is tasked to steer the SOE in line with the agreed performance indicators and targets with its shareholder. The accounting authority must ensure that the SOE has and maintains an internal control environment that conforms to the Public Finance Management Act and the Companies Act, guided by good corporate governance practices.

The tone at the top set by the accounting authority of an SOE together with its shareholder is therefore of utmost importance, as this has a direct impact on whether the SOE is steered in the right strategic direction. The accounting authority must implement and monitor policies to evaluate the performance of those tasked with implementation against the agreed performance objectives. Legislation requires **accounting authorities** to monitor the performance against the set targets and take corrective action on a timely basis **to establish a stable environment where accountability becomes responsibility**.

Failures in this regard have resulted in government having to assist most SOEs in order for them to remain sustainable. These failures and the state of affairs of SOEs have also received a lot of attention from commissions of inquiry, media reports, and credit-rating agencies.

This section provides some context to the state of the internal controls prevailing at our SOEs, providing a picture of each SOE's audit outcomes over the last five years and looking at the status of key focus areas such as financial health, compliance with legislation as well as stability in key management and oversight positions. The section also considers the status of the strategic oversight provided by the SOEs' shareholder departments and executive authorities.

We are currently responsible for the external audits of 14 of the 21 SOEs (67%), compared to only eight (38%)

five years ago. Six SOEs are audited by other audit firms. Telkom is not considered a public entity that falls under our mandate and is therefore not included in our analysis. During 2018-19, the 20 SOEs that we deal with in this report (both those audited by us and by audit firms) had a combined total estimated expenditure (operational and capital expenditure) of R347 billion – compared to the total estimated expenditure budget of R1 747 billion for public entities, other institutions and departments.

Our audits for the year ended 31 March 2019 at South African Airways (as well as for the financial year ended 31 March 2018), the South African Nuclear Energy Corporation and Trans-Caledon Tunnel Authority had not been finalised for purposes of this section by 30 September 2019.

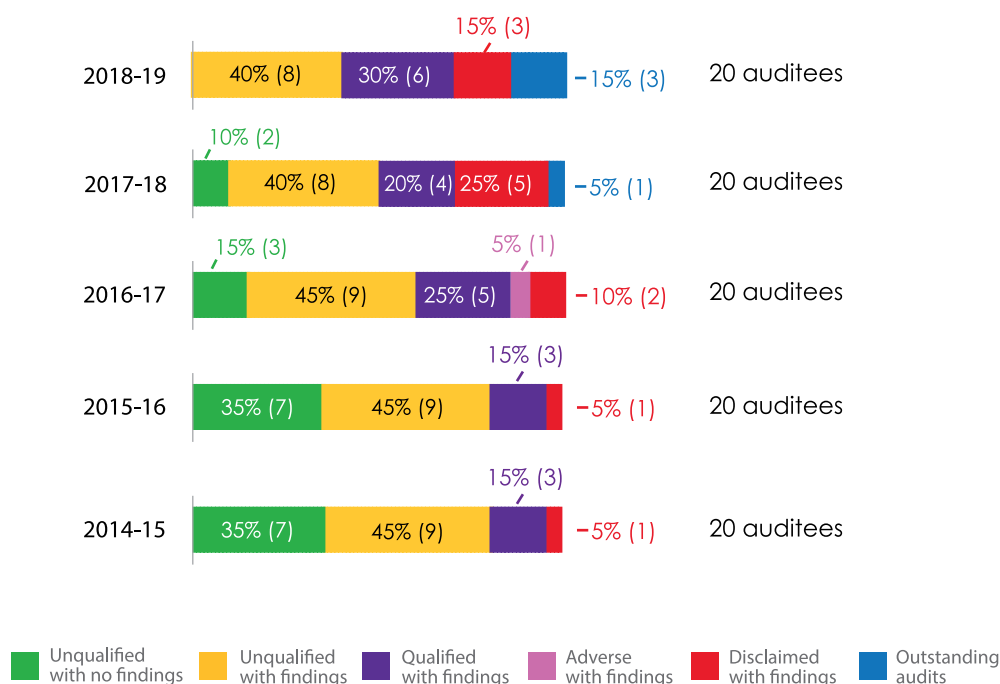
Please note that the analysis and detailed audit outcomes per SOE are provided at group level in those instances where the SOE consists of a group of companies. In the individual summaries, the information on audit outcomes, financial health as well as vacancies and stability relates to the holding company as a stand-alone entity, while the information on irregular expenditure and supply chain management pertains to the group as a whole. The audit outcomes of the individual subsidiaries of the SOEs are provided in the annexure to the general report available on our website.

## OVERALL AUDIT OUTCOMES

The overall audit outcomes of the SOEs regressed when compared to the previous year and significantly regressed over the last five years. Confidence in the ability of the executives tasked to manage the affairs of SOEs has similarly regressed over the past years. Turnaround plans initiated almost on an annual basis had almost no impact in restoring the SOE environment, as executive and management instability makes it impossible to hold those responsible accountable. We found the discipline of sustained monitoring and oversight of key controls to be extremely weak at most SOEs. **The overall audit outcomes of the SOEs are the worst they have ever been.**

Renewed efforts to turn around the dire state of affairs at SOEs have begun with the appointment of new accounting authorities at most SOEs. There was a significant increase in irregular expenditure at these SOEs due to a drive to clean up irregularities from the past. We provide more details in this regard throughout the section to serve as an example to all auditees to implement similar measures to improve their internal controls and clear irregularities.

Similar to the previous year, the overall audit outcomes again regressed with the less desirable audit outcomes (qualified and disclaimed) increasing, as shown below:



The picture over the last five years has deteriorated significantly with none of the SOEs being able to achieve an unqualified audit outcome with no findings (clean audit) in the current year. Below we look at the reasons for the overall audit outcomes.

## CAUSE OF THE AUDIT OUTCOMES

### FINANCIAL STATEMENTS

The financial statements submitted to the external auditors by all SOEs were in a worse condition than a year ago. This is because **only 18%** (three of the 17 SOEs with completed audits) **submitted financial statements for auditing without material misstatements**. Of the 12 SOEs that submitted financial statements of a poor quality, only six could correct all the material misstatements that the auditors identified during the audit, resulting in only 47% of the SOEs with completed audits receiving unqualified audit opinions.

### NON-COMPLIANCE WITH LEGISLATION RELATING TO FINANCIAL MANAGEMENT

**Material non-compliance with legislation** by SOEs and their significant subsidiaries again **increased** – from 89% to 94%. Overall, the main areas of non-compliance were the poor quality of the financial statements, supply chain management weaknesses, and irregular as well as fruitless and wasteful expenditure not being prevented.

It is of utmost importance that SOEs provide credible information in their financial statements and that they comply with key legislation in order to provide confidence in their ability to stimulate the industry as mandated – and ultimately grow the South African economy. Doubt about the financial statements and level of compliance with legislation affects the considerations that rating agencies take into account when deciding on a rating for that specific SOE and the overall rating of the South African fiscus.

Based on our audits, the following key causes resulted in the poor financial management at our SOEs:

#### Regression from unqualified opinion with no findings

The Development Bank of Southern Africa and the Industrial Development Corporation regressed from a clean audit to an unqualified opinion with findings on compliance matters in relation to procurement and the quality of its submitted financial statements, respectively. SOEs should address the following internal control deficiencies:

- Monitoring compliance with relevant legislation should be a key control on a daily basis.
- SOEs in general need to report their financial statements in terms of the International Financial Reporting Standards. Due to the ever-changing reporting requirements and updated and new standards being introduced, it is important for SOEs to keep up to date with these reporting changes and plan for them well in advance.

## Financially unqualified opinion with findings

Non-compliance with key legislation was common in the following three areas:

- Material misstatements in the financial statements submitted for auditing were subsequently corrected to avoid a qualification. In most instances, SOEs either responded too late or did not have appropriate plans to successfully implement the new revenue and financial instruments standards (International Financial Reporting Standards 15 and 9, respectively), causing material misstatements that were subsequently corrected.
- The Public Finance Management Act directs accounting authorities to prevent the incurrence of irregular as well as fruitless and wasteful expenditure. In most instances, SOEs were not able to prevent such expenditure. In this regard, irregular expenditure increased significantly to R58 billion from R30 billion in the previous year due to a drive to clean up prior irregularities.

- SOEs struggled to comply with legislative requirements regarding supply chain management when procuring goods and services. Together with a lack of corrective action against those responsible for such non-compliance as provided for in legislation, this created an environment in which the disrespect for rules and policies was not appropriately disciplined.

### Qualified opinion

- The completeness of irregular expenditure was the main cause of most of the qualifications reported. This has had a negative impact on the audit outcomes of a couple of SOEs over the last three audit cycles (Eskom, South African Forestry Company and Transnet).
- In other instances, the cause of the qualifications was mostly due to instances where complex transactions were entered into but the accounting thereof in the financial statements was not properly considered beforehand.

The top five contributors to the significant increase in the irregular expenditure were:

SOE	Irregular expenditure incurred in 2018-19	Movement
Transnet	R49 922 million	Increased*
Eskom	R6 618 million	Decreased
South African Broadcasting Corporation	R351 million	Decreased
Airports Company of South Africa	R264 million	Decreased
Denel	R217 million	Decreased

\* Most of the irregular expenditure disclosed in the financial statements of Transnet was caused by non-compliance with the Preferential Procurement Policy Framework Act and its regulations. Irregular expenditure of R41,5 billion was incurred on the contracts with different suppliers for 1 064, 95 and 100 locomotives.

### Disclaimed opinion

- As mentioned earlier, the financial reporting framework mostly used by SOEs is the International Financial Reporting Standards, which requires the entity to report on its financial results on the principle that it will continue to operate in the foreseeable future (normally a 12-month period from the end of its reporting period). Most SOEs in this category had difficulty in providing the auditors with clear evidence that they would be able to pay debts as they became due in the next 12 months. Combined with other uncertainties, such as significant dependencies on government

for support, declining economic conditions and a lack of customer confidence in the SOEs, this prevented us from concluding on the reasonability and appropriateness of the application of the going concern principle.

- At Denel and South African Express Airways, significant weaknesses in internal controls were the main drivers of the disclaimed audit opinion. In the absence of a strong internal control environment, management was unable to produce credible financial statements.

The cause of the audit outcomes is further analysed in the individual SOE summaries later on in this section.

## FINANCIAL HEALTH OF STATE-OWNED ENTITIES

We mentioned earlier that SOEs are independent entities that are partially or fully owned by the state to achieve various socio-economic goals. They are expected to fulfil a dual commercial and developmental role. The **economic conditions** in which these SOEs need to operate **have worsened over the last five years**. Government has committed to support the SOEs in various forums, such as through the finance

minister's budget speech in February 2019. Since the budget had been tabled in Parliament, various financial support initiatives were extended to SOEs such as Eskom, the South African Broadcasting Corporation, South African Airways, Denel and South African Express Airways. More detail on the support provided to these SOEs can be found in the individual SOE summaries.



### What does it mean to give a guarantee to an SOE by the state?

By granting a guarantee, the state is 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 a commitment by the state to take responsibility for a loan in the event of default by the SOE.

Providing a guarantee is not necessarily negative, such as when government decides to provide support to an SOE established in a specific industry or sector, due to that key industry or sector struggling to grow as expected in the South African economy.

These guarantees can be a direct charge to the National Revenue Fund should the SOEs default on their guarantee liabilities. Records of guarantees issued and the total exposure to government are kept by the fund.

**Government provided financial guarantees amounting to R446 billion** (2017-18: R428 billion) to 11 of the SOEs (2017-18: 10). The total government exposure relating to these guarantees amounted to R328 billion (2017-18: R290 billion) – SOEs therefore used 13% more of the guarantees in the current financial year than in the previous year. Of the total guarantees, 78% was provided to Eskom, with the total cumulative guarantees issued to Eskom amounting to R350 billion (2017-18: R350 billion), with a R286 billion (2017-18: R245 billion) exposure as at 31 March 2019 – a 17% increase in the utilisation of the guarantees. The amount stated as total exposure means that the SOEs utilised the guarantees to obtain loans from lenders.

Even despite the difficult economic conditions, it is commendable that some SOEs sustained their operations and fulfilled their dual mandate with their own resources, with minimal or no support from government. The key enablers to SOEs being able to sustain themselves are often found in leadership stability, well-considered performance plans, key financial ratios that are monitored to avoid falling behind on financial management responsibilities, and those charged with governance and oversight holding officials accountable for commitments and periodically monitoring SOEs' performance against predetermined objectives.

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## INDIVIDUAL SUMMARIES OF STATE-OWNED ENTITIES

On the following pages, we provide a snapshot of the key audit considerations per SOE. We first look at the SOEs that we audit and then focus on those audited by other audit firms. Please note that the financial health

indicators consist of only the information reported in the audit reports, and are therefore excluded from the summaries of those SOEs of which the audits are performed by audit firms.





# Airports Company South Africa (Acsa)

(Audited by AGSA)

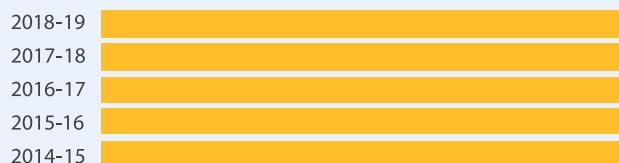


Overall stagnation in audit outcome



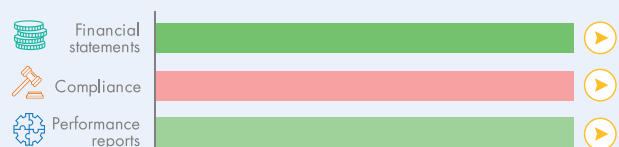
## Audit outcomes

Overall stagnation due to material non-compliance relating to supply chain management and material adjustments to financial statements



■ Unqualified with no findings 
 ■ Unqualified with findings 
 ■ Qualified with findings 
 ■ Adverse with findings 
 ■ Disclaimed with findings 
 ■ Outstanding audits

## Audit outcomes on three key areas



**Financial statements:** Audit opinion on financial statements was unqualified due to Acsa correcting the material misstatements identified

**Compliance:** Material non-compliance relating to quality of financial statements, procurement and contract management, effecting consequences as well as expenditure management (failure to take steps to prevent the incurrence of irregular and fruitless and wasteful expenditure)

**Performance reports:** No material findings or misstatements

■ Unqualified 
 ■ Qualified 
 ■ Disclaimed 
 ■ With no findings 
 ■ With findings



## Irregular expenditure



R264 million

R400 million



2018-19

Identified by auditees



2017-18

Identified during audit

No irregular expenditure incurred in prior years – identified in current year



## Financial health

### Going concern status



Good

Of concern

Intervention required

Section 51(1)(d)(i) and (iii) of the PFMA sets responsibilities for the accounting authority to collect all revenue due and manage available working capital efficiently and economically. The effectiveness of Acsa in managing the collection of revenue, not being dependent on a specific revenue stream and also monitoring their budget, contributed to them not facing going concern challenges.

### Financial health indicators

More than 10% of debt irrecoverable



## Findings on supply chain management



■ With no findings 
 ■ With material findings

Lack of competitiveness in the procurement of some goods, works and services. Certain contracts awarded to bidders based on pre-qualification criteria that differed from those stipulated in original invitation for bidding. Lack of evidence to confirm that certain construction contracts were awarded to contractors registered with Construction Industry Development Board. Root causes of non-compliance matters were slow response in implementing commitments to capacitate supply chain management unit with appropriately skilled and experienced staff to monitor compliance as well as lack of implementation of consequences.



## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Vacant for less than 6 months
Chief financial officer	Vacant for more than 6 months

Stability (average number of months in position)

Chief executive officer	Vacant
Chief financial officer	Vacant





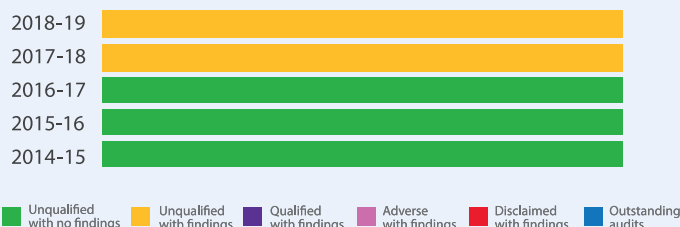


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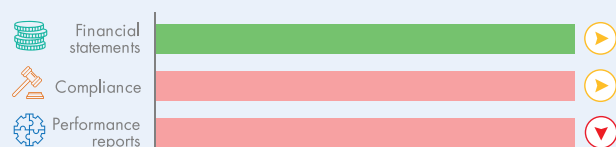


## Audit outcomes

Overall stagnation in audit outcome on unqualified with findings as a result of material adjustments to financial statements and one material finding on performance report in 2018-19; for 2017-18, the finding was due to not preventing irregular expenditure



## Audit outcomes on three key areas



**Financial statements:** Unqualified

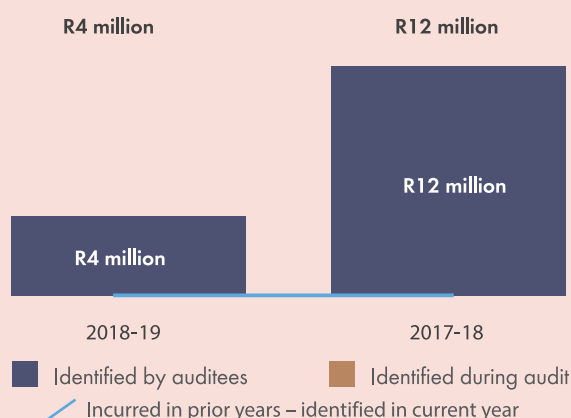
**Compliance:** Material non-compliance due to quality of financial statements as material adjustments were required to avoid a qualification

**Performance reports:** Material finding relating to a limitation on one goal due to performance processes not being established to validate achieved percentage received from third party

Unqualified Qualified Disclaimed With no findings With findings



## Irregular expenditure



Of the R4 million irregular expenditure for 2018-19, R0,2 million was identified during the audit

The irregular expenditure incurred in prior years – identified in current year amounted to an insignificant amount of R52 000 in 2018-19 and R123 000 in 2017-18



## Vacancies and stability

Vacancies at year-end	Accounting authority	No vacancies
	Chief executive officer	Not vacant
	Chief financial officer	Not vacant



## Financial health

### Going concern status



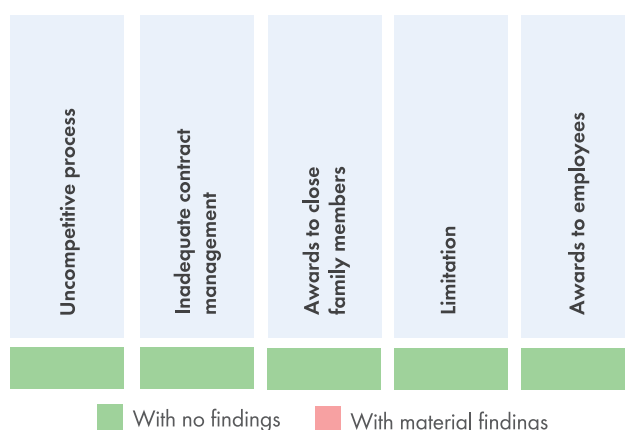
No material uncertainty on going concern evident

- Good
- Of concern
- Intervention required

### Financial health indicators



## Findings on supply chain management



No material non-compliance findings with regard to supply chain management





# Central Energy Fund (CEF)

(Audited by AGSA)

Subsidiaries: Petroleum Oil and Gas Corporation of South Africa, SFF Association, South African Agency for Promotion of Petroleum Exploration and Exploitation

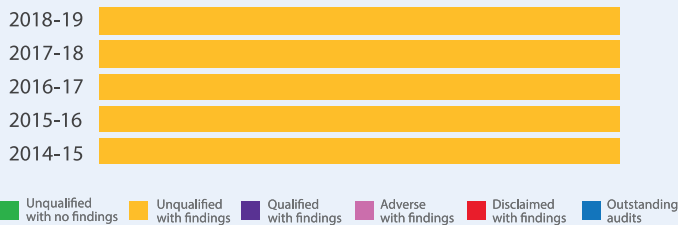


Overall stagnation in audit outcome

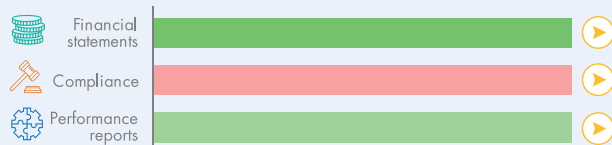


## Audit outcomes

### Stagnation over past five years



### Audit outcomes on three key areas



**Financial statements:** No material findings reported

**Compliance:** Findings on quality of financial statements, strategic planning and performance management, expenditure management as well as effecting consequences

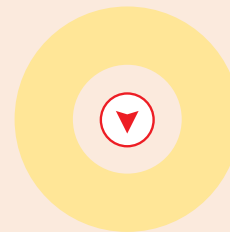
**Performance reports:** No material findings reported

Legend: Unqualified (Green), Qualified (Purple), Disclaimed (Red), With no findings (Light Green), With findings (Pink)

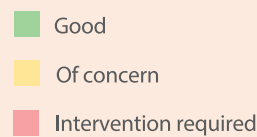


## Financial health

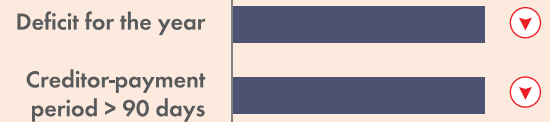
### Going concern status



Concerning due to net loss of R470 million and creditor-payment period of 296 days



### Financial health indicators



## Irregular expenditure



R20 million

R17 million



2018-19



2017-18

Identified by auditees

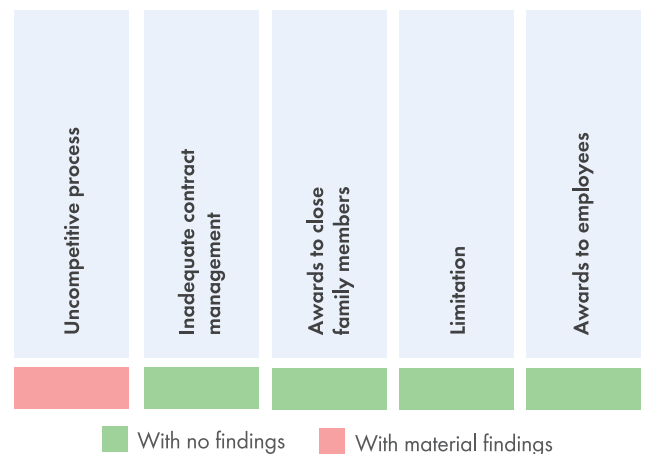
Identified during audit

No irregular expenditure incurred in prior years – identified in current year

The irregular expenditure incurred by the group consists of R8,4 million by CEF and R11,8 million by subsidiary (African Exploration Mining and Finance Corporation)



## Findings on supply chain management



Non-compliance with supply chain management policy to ensure that minimum of three quotations was obtained. Non-adherence to Preferential Procurement Regulations as bidders were evaluated based on pre-qualification criteria that differed from original bid invitation.



## Vacancies and stability

Vacancies at year-end

Accounting authority	3 vacancies for less than 6 months and 1 vacancy for more than 6 months
Chief executive officer	Vacant for more than 6 months
Chief financial officer	Not vacant

Stability (average number of months in position)

Chief executive officer	Vacant
Chief financial officer	24







Denel

(Audited by AGSA)

Subsidiaries: Denel Saab Aerostructures, Denel Vehicle Systems, Densecure, LMT Holdings, LMT Products, Turbomeca Africa



Overall stagnation in audit outcome



## Audit outcomes

Remained disclaimed due to significant weaknesses in internal control



Unqualified with no findings Unqualified with findings Qualified with findings Adverse with findings Disclaimed with findings Outstanding audits

## Audit outcomes on three key areas



**Financial statements:** Disclaimed opinion on revenue, inventory, trade and other receivables, trade and other payables, property, plant and equipment, investment in subsidiaries, retirement benefit obligation, operating expenditure, contingent liabilities, prior period errors, risk management disclosure, related parties, irregular and fruitless and wasteful expenditure as well as deferred and income tax

**Compliance:** Material findings on quality of financial statements, expenditure management, revenue management, strategic planning, procurement and contract management as well as effecting consequences

**Performance reports:** Material findings on both reliability and usefulness

Unqualified Qualified Disclaimed With no findings With findings



## Irregular expenditure



R217 million

R406 million



2018-19

Identified by auditees



2017-18

Identified during audit

No irregular expenditure incurred in prior years – identified in current year

Full extent of irregular expenditure could not be confirmed as per our basis for disclaimed opinion



## Vacancies and stability

Vacancies at year-end

Accounting authority No vacancies  
Chief executive officer Not vacant  
Chief financial officer\* Vacant for less than 6 months

\*Appointed in September 2019



## Financial health

### Going concern status



Financial viability remains a significant concern due to adverse liquidity ratios and significant operating losses, resulting in material uncertainty regarding going concern

Good  
Of concern  
Intervention required

### Financial health indicators

Material uncertainty regarding going concern



## Findings on supply chain management



With no findings With material findings

Non-adherence to supply chain management policy to ensure that a minimum of three quotations was obtained and that a competitive bidding process was followed where required approval for deviation was obtained. Non-adherence to Preferential Procurement Policy Framework Act and its regulations, as bid invitations did not include functionality criteria to ensure a fair procurement process. Construction contracts were entered into without verifying that supplier was registered with CIDB.



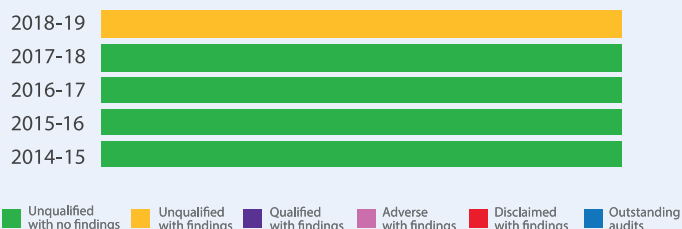


(Audited by AGSA)

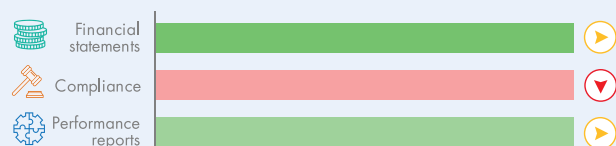


## Audit outcomes

Overall regression due to material non-compliance with legislation on supply chain management



## Audit outcomes on three key areas



**Financial statements:** Financial statements submitted were free of material misstatements

**Compliance:** Material non-compliance relating to preferential procurement prescripts on procurement of local content and production of goods and services from designated sectors

**Performance reports:** Material misstatements on reliability, which were subsequently corrected by management

Legend: Unqualified (Green), Qualified (Purple), Disclaimed (Red), With no findings (Light Green), With findings (Pink)



## Irregular expenditure



R0,4 million

R0 million



2018-19

2017-18

Identified by auditees

Identified during audit

No irregular expenditure incurred in prior years – identified in current year

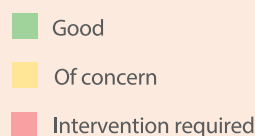


## Financial health

### Going concern status



No material uncertainty on going concern evident

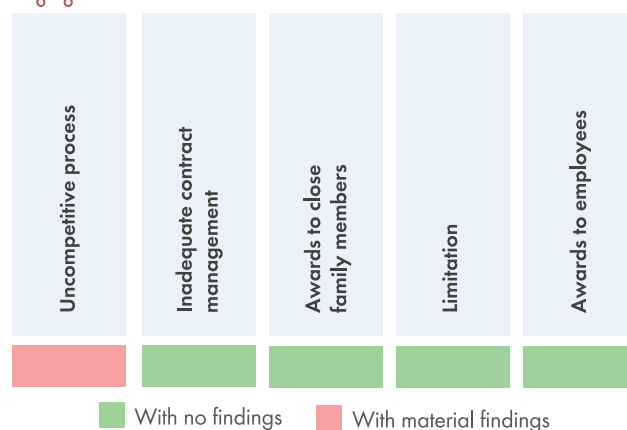


### Financial health indicators

The financial health of DBSA is assessed on specific industry ratios as reported in its annual report.



## Findings on supply chain management



Non-compliance due to procurement of goods and services from designated sectors without following preferential procurement prescripts relating to local production and content in Infrastructure Delivery Division where DBSA acts as implementing agent on behalf of other government entities.



## Vacancies and stability

Vacancies at year-end

Accounting authority	4 vacancies for less than 6 months
Chief executive officer	Not vacant
Chief financial officer	Not vacant

Stability (average number of months in position)





# Independent Development Trust (IDT)

(Audited by AGSA)

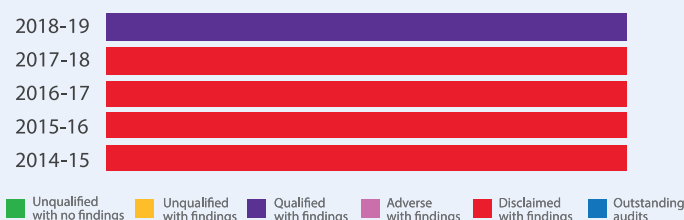


Overall improvement in audit outcome

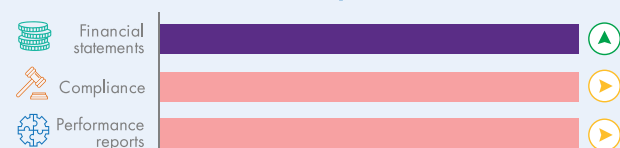


## Audit outcomes

Improved from disclaimed to qualified due to enhanced record management; significant internal control deficiencies remain to be addressed to prevent a regression in future



### Audit outcomes on three key areas



**Financial statements:** Qualifications on corresponding figures of programme assets and liabilities as well as revenue and receivables from exchange transactions; additionally, there was an impact on disclosure notes relating to first-time adoption of SA Standards of Generally Recognised Accounting Practice and prior year adjustments

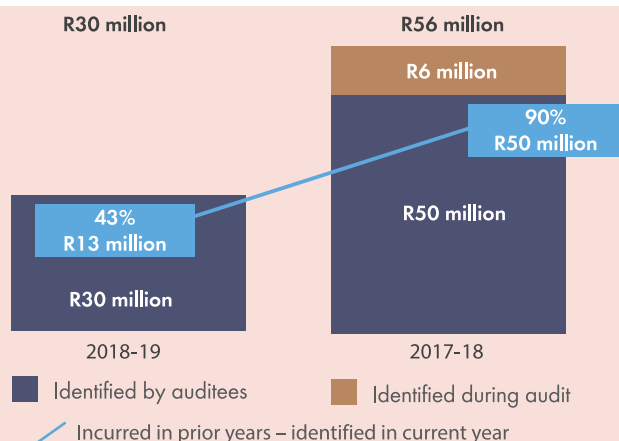
**Compliance:** Findings on quality of financial statements and performance report, revenue management, expenditure management, effecting consequences as well as procurement and contract management

**Performance reports:** Material findings on reliability of reported achievements in both current and previous year

Legend: Unqualified (Green), Qualified (Purple), Disclaimed (Red), With no findings (Light Green), With findings (Pink)



## Irregular expenditure



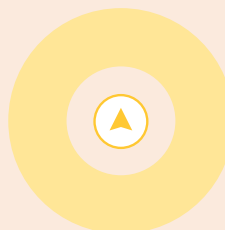
Of the R30 million irregular expenditure for 2018-19, R0.4 million was identified during the audit

The IDT is an implementing agent and the irregular expenditure reflected relates to overhead costs only – we identified additional irregular expenditure of R73,7 million incurred by the IDT on behalf of its client departments

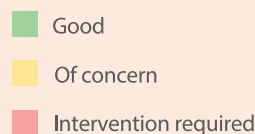


## Financial health

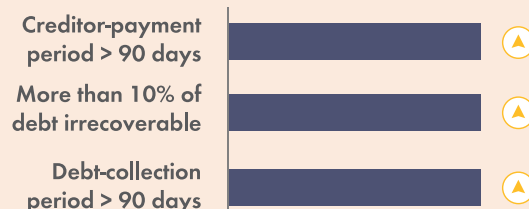
### Going concern status



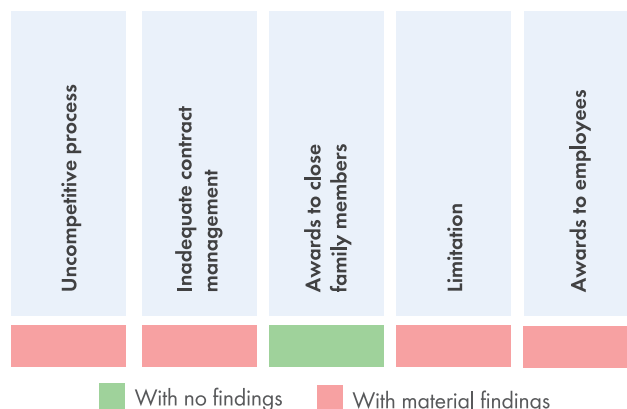
Before 2018-19, we could not perform a meaningful financial health analysis due to the repetitive disclaimed audit opinions on the financial statements. Even though we identified no material going concern uncertainty for 2018-19, the IDT still needs to attend to serious concerns as evidenced by the negative indicators below.



### Financial health indicators



## Findings on supply chain management

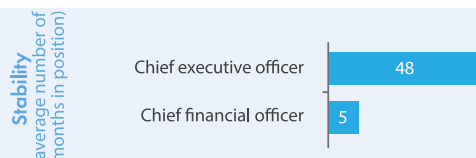


IDT did not procure some goods, works or services through a procurement process that was fair, equitable, transparent and competitive – similar to the previous year. The absence of appropriate consequences, lack of human resource capacity in supply chain management unit as well as outdated policies and procedures contributed to lack of improvement in this area.



## Vacancies and stability

Vacancies at year-end	Accounting authority	8 vacancies for more than 6 months
	Chief executive officer	Not vacant
	Chief financial officer	Not vacant





# Land and Agricultural Development Bank of South Africa (Land Bank)

(Audited by AGSA)

Subsidiaries: Land Bank Insurance, Land Bank Life Insurance

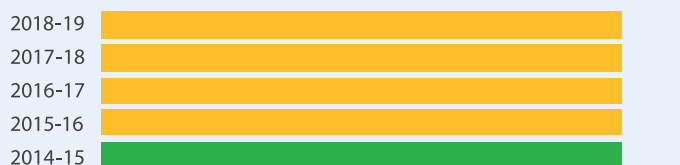


Overall stagnation in audit outcome



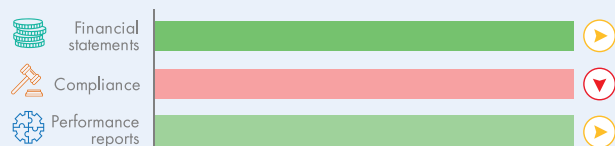
## Audit outcomes

Remained stagnant on unqualified with findings on compliance with legislation due to failure to submit financial statements that were free from misstatements



Legend: Unqualified with no findings (green), Unqualified with findings (yellow), Qualified with findings (purple), Adverse with findings (pink), Disclaimed with findings (red), Outstanding audits (blue)

## Audit outcomes on three key areas



**Financial statements:** Financial statements contained material misstatements relating to loans by credit quality and collateral values of loans issued, which were subsequently corrected by management

**Compliance:** Material non-compliance relating to preparation of financial statements in line with applicable accounting framework due to material misstatements in financial statements submitted for auditing

**Performance reports:** Material misstatements on reliability, which were subsequently corrected by management

Legend: Unqualified (green), Qualified (purple), Disclaimed (red), With no findings (light green), With findings (pink)



## Financial health

### Going concern status



No material uncertainty on going concern evident

Legend: Good (green), Of concern (yellow), Intervention required (pink)

### Financial health indicators

The financial health of Land Bank is assessed on specific industry ratios as reported in its annual report.



## Irregular expenditure



R0,14 million

R2,080 million

R2,080 million

R0,14 million

2018-19

2017-18

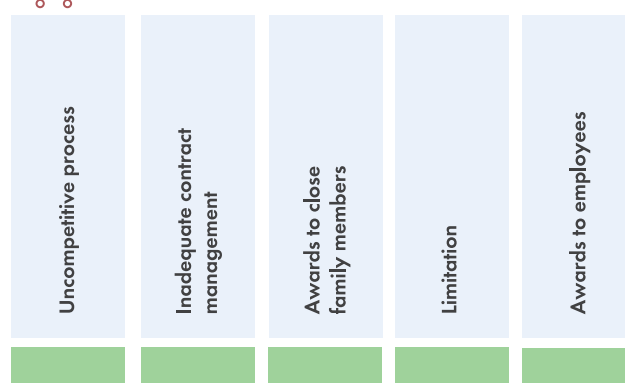
Identified by auditees

Identified during audit

No irregular expenditure incurred in prior years – identified in current year



## Findings on supply chain management



Legend: With no findings (green), With material findings (pink)

No material non-compliance findings with regard to supply chain management



## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Vacant for less than 6 months
Chief financial officer*	Not vacant

Stability (average number of months in position)

Chief executive officer	Vacant
Chief financial officer*	45

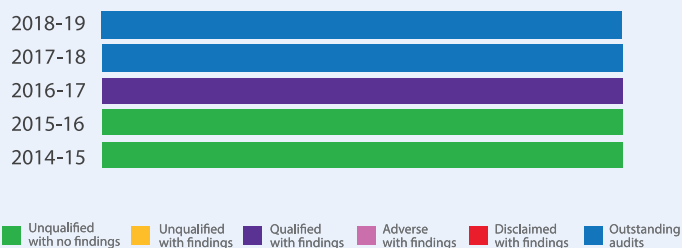
\* Chief financial officer resigned after year-end in May 2019 after 45 months in position





## Audit outcomes

Regressed in 2016-17 to qualified opinion, while current and previous year audits are still outstanding because of non-submission of financial statements for auditing



## Audit outcomes on three key areas



Current and previous year audits are still outstanding

Outstanding audit



## Irregular expenditure

Unknown

2018-19

2017-18

Outstanding audit

No irregular expenditure reported in either year as financial statements were not submitted

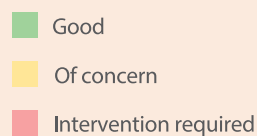


## Financial health

### Going concern status



SAA has not been able to submit financial statements due to liquidity constraints. Loans have matured and could not be repaid. Ongoing negotiations with lenders to extend current debt is in progress.

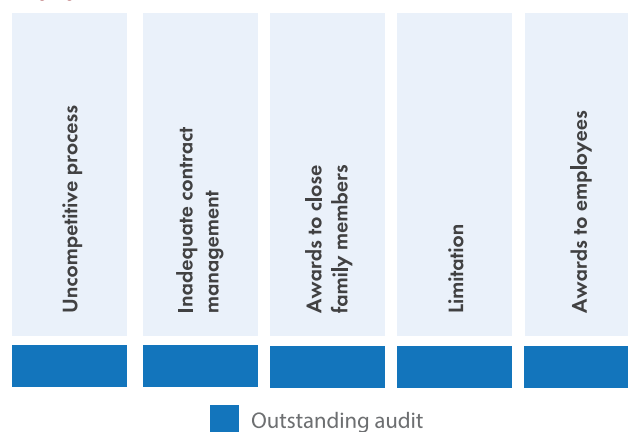


### Financial health indicators

Material uncertainty regarding going concern



## Findings on supply chain management



## Vacancies and stability

Vacancies at year-end

Accounting authority*	1 vacancy for more than 6 months
Chief executive officer**	Vacant for less than 6 months
Chief financial officer	Vacant for more than 6 months

Stability (average number of months in position)

No stability in key positions

\* Chair of the board resigned in July 2019

\*\* Chief executive officer resigned in June 2019



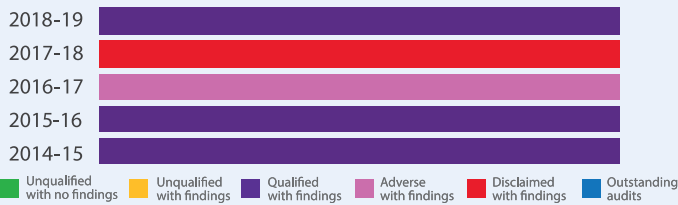


(Audited by AGSA)

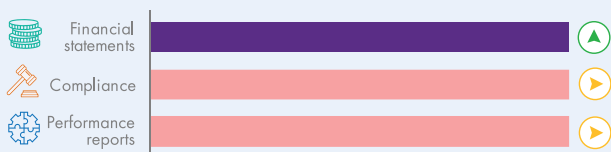


## Audit outcomes

Audit outcome improved primarily due to funding made available through Department of Communications, subject to certain conditions being met



### Audit outcomes on three key areas



**Financial statements:** Qualifications on property, plant and equipment as well as irregular expenditure

**Compliance:** Findings on quality of financial statements, revenue management, expenditure management, effecting consequences as well as procurement and contract management

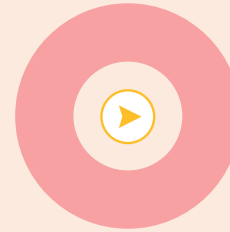
**Performance reports:** Material findings on reliability in the current year, and both usefulness and reliability in previous year

Unqualified Qualified Disclaimed With no findings With findings



## Financial health

### Going concern status

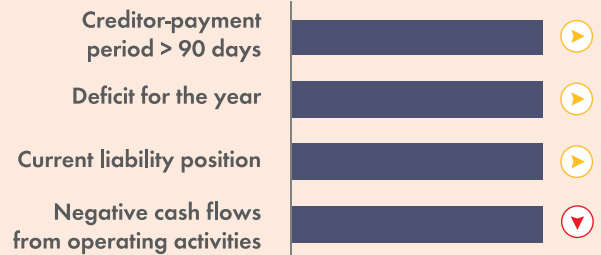


Material uncertainty on going concern due to loss of R482 million (2017-18: R744 million) and current liabilities exceeding current assets by R875 million at year-end (2017-18: R456 million). Trade and other payables increased to R1,6 billion from R1,1 billion in 2017-18.

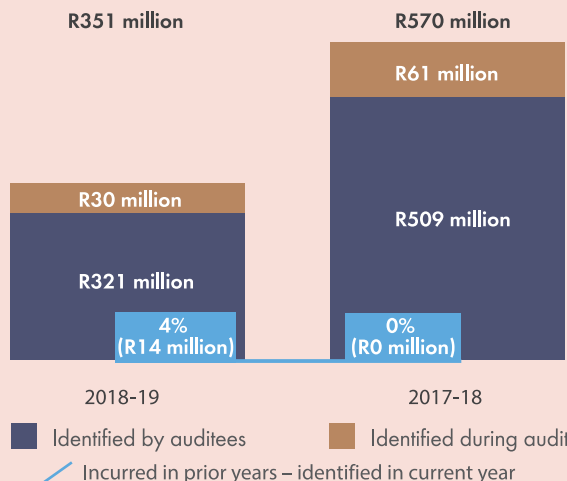
Government funding in the form of a bailout has been made available to the Department of Communications, which will be provided to the SABC subject to certain conditions being met (including the review and finalisation of turnaround strategy).

- Good
- Of concern
- Intervention required

### Financial health indicators



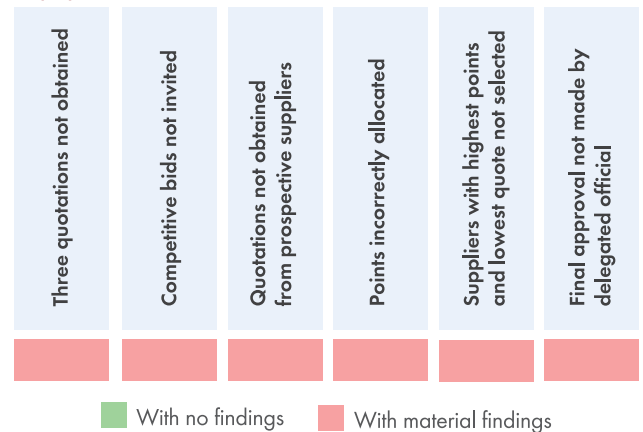
## Irregular expenditure



Full extent of irregular expenditure could not be confirmed as per our basis for qualified opinion



## Findings on supply chain management

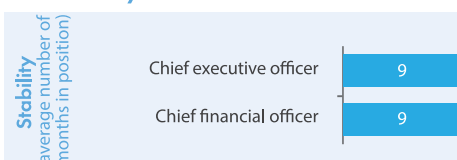


The SABC continued to have material findings on procurement. The head of the supply chain management unit was suspended and subsequently dismissed during the year and the position remains vacant to date. Supply chain management staff lacked the necessary skills and competence to implement supply chain management policy and comply with necessary supply chain management requirements.



## Vacancies and stability

Accounting authority	Board was not quorate for 4 months
Chief executive officer	Not vacant
Chief financial officer	Not vacant







# South African Express Airways (SAX)

(Audited by AGSA)

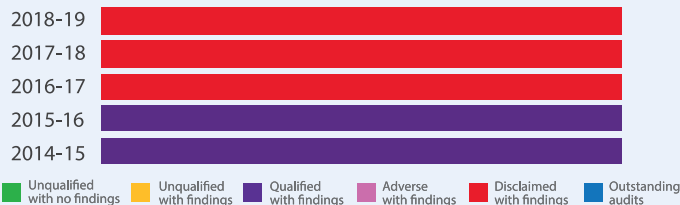


Overall stagnation in audit outcome



## Audit outcomes

Remained stagnant on disclaimed due to lack of adequate implementation of action plans to correct prior year qualification areas and going concern issues



## Audit outcomes on three key areas



**Financial statements:** Material misstatements / limitations relating to property, plant and equipment, inventories, trade and other receivables, trade and other payables, provisions, other financial liabilities, revenue, other operating expenses, gains of foreign exchange adjustments, finance costs, effects on taxation, contingencies, related parties, directors' emoluments, financial instruments, prior period error, new standards as well as irregular and fruitless and wasteful expenditure

**Compliance:** Findings on quality of financial statements, revenue management, expenditure management, liability management, strategic planning and performance management, effecting consequences as well as procurement and contract management

**Performance reports:** Material limitation as no performance report was prepared

Legend: Unqualified (green), Qualified (purple), Disclaimed (red), With no findings (light green), With findings (pink)



## Irregular expenditure



R156 million

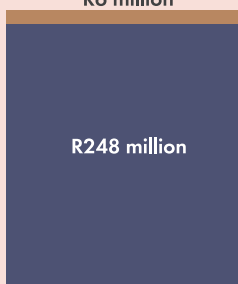


2018-19

Identified by auditees

R254 million

R6 million



2017-18

Identified during audit

No irregular expenditure incurred in prior years – identified in current year

Full extent of irregular expenditure could not be confirmed as per our basis for disclaimed opinion



## Vacancies and stability

Vacancies at year-end	Accounting authority	No vacancies
	Chief executive officer	Vacant for more than 6 months
	Chief financial officer*	Vacant for more than 6 months

\* A permanent chief financial officer was appointed after year-end



## Financial health

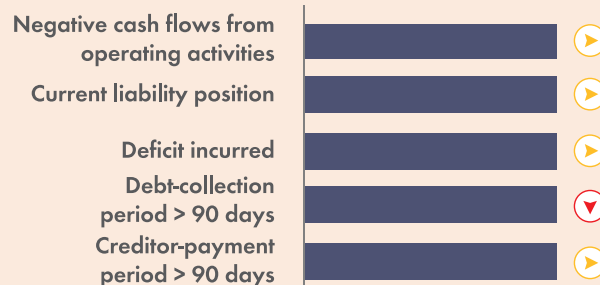
### Going concern status



Material uncertainty relating to going concern due to loss of R591 million (2017-18: R162 million); current liabilities exceeding current assets by R374 million; and net cash from operating activities further deteriorating to negative R461 876 782 (2017-18: -R101 566 324). This was further affected by possible loss of market due to grounding during the financial year. SAX received a R300 million injection, which replaced the government guarantee previously issued. No turnaround strategy was provided.

- Good (green)
- Of concern (yellow)
- Intervention required (red)

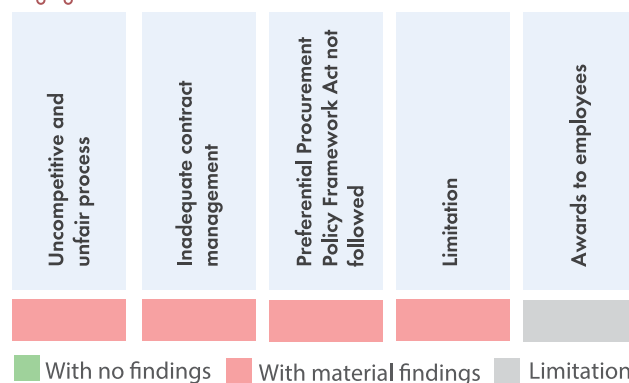
### Financial health indicators



The poor payment days were due to liquidity issues at SAX. Most of the debtors balance is South African Airways, hence the inability to collect.



## Findings on supply chain management



Legend: With no findings (green), With material findings (red), Limitation (grey)

SAX continued to have material findings on procurement, mainly due to non-adherence to supply chain management policy to ensure that minimum of three quotations was obtained and that competitive bidding process was followed. The head of procurement position was vacant during the year and remains vacant to date. Supply chain management staff lacked the necessary skills and competence to implement supply chain management policy.





# South African Forestry Company (Safcol)



Overall stagnation in audit outcome

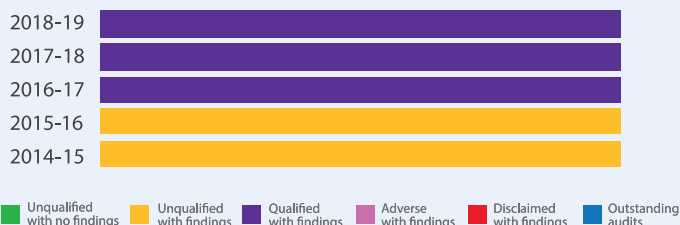
(Audited by AGSA)

Subsidiary: Komatiland Forests

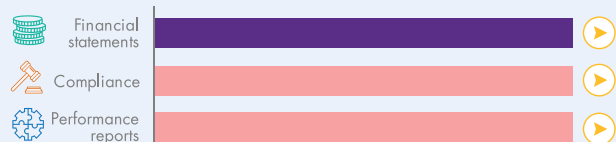


## Audit outcomes

Remained stagnant from previous year, but reduction in qualification areas from 9 to only 1



## Audit outcomes on three key areas



**Financial statements:** Qualification on irregular expenditure

**Compliance:** Findings on quality of financial statements, expenditure management as well as effecting consequences

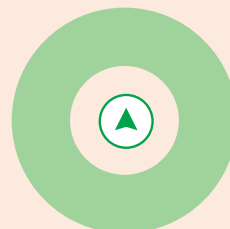
**Performance reports:** Material findings on reliability in current year

Unqualified Qualified Disclaimed With no findings With findings



## Financial health

### Going concern status



The group had negative cash flows from operating activities in the previous year, which have since returned to positive operating cash flows

- Good
- Of concern
- Intervention required

### Financial health indicators

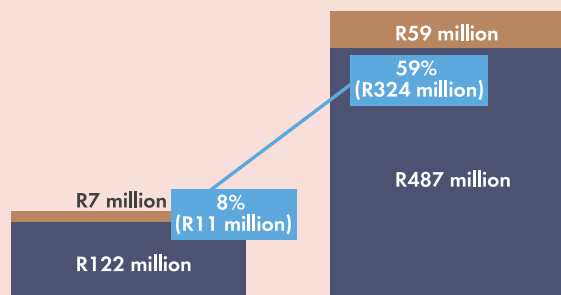


## Irregular expenditure



R129 million

R546 million



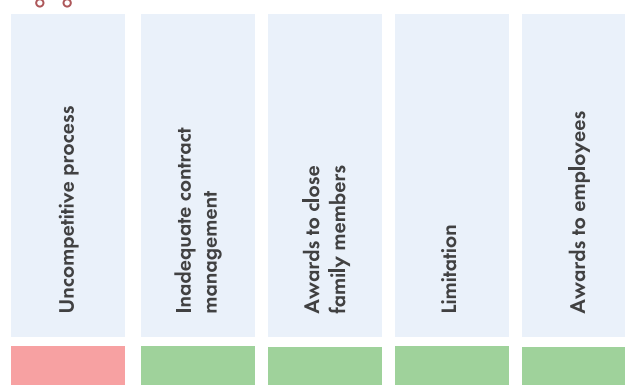
2018-19

2017-18

Identified by auditees Identified during audit Incurred in prior years – identified in current year



## Findings on supply chain management



With no findings With material findings

Effective and appropriate measures were not timeously implemented to prevent and detect non-compliance with legislation.



## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Not vacant
Chief financial officer	Vacant for less than 6 months

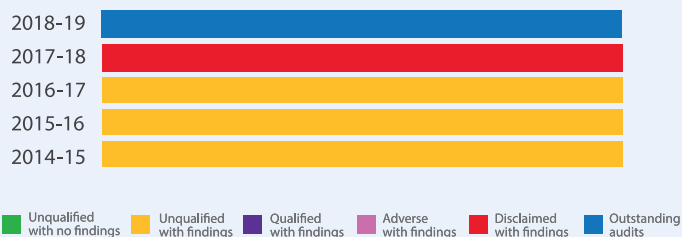
Stability (average number of months in position)



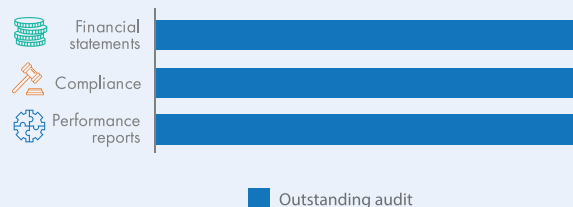


## Audit outcomes

Regressed in 2017-18 to disclaimed opinion, while current year's audit is outstanding due to late submission of financial statements



## Audit outcomes on three key areas

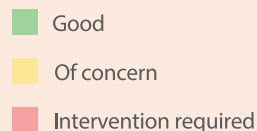


## Financial health

### Going concern status



Sufficient appropriate audit evidence could not be provided that the group was a going concern



### Financial health indicators

Material uncertainty regarding going concern



129



## Irregular expenditure

Unknown R0 million

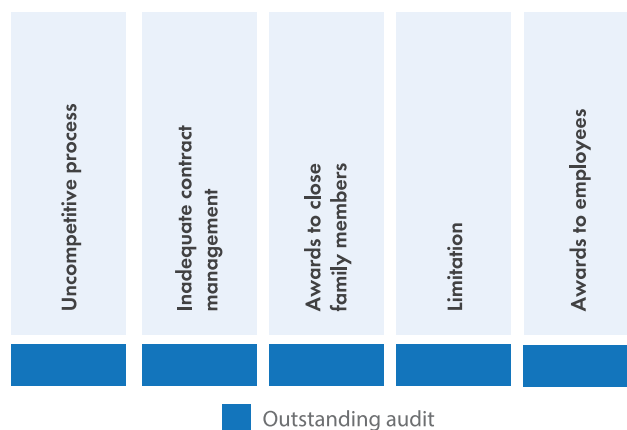
2018-19 R0 million  
2017-18 R0 million

Outstanding audit

No irregular expenditure reported in 2017-18



## Findings on supply chain management

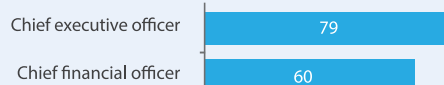


## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Not vacant
Chief financial officer	Not vacant

Stability (average number of months in position)





# South African Post Office (Sapo)

(Audited by AGSA)

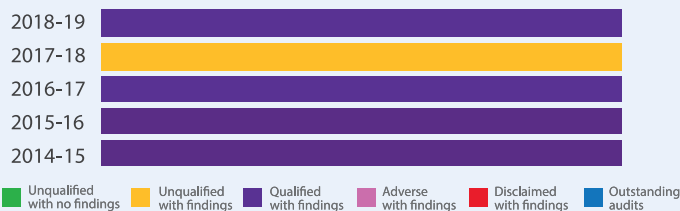


Overall regression in audit outcome

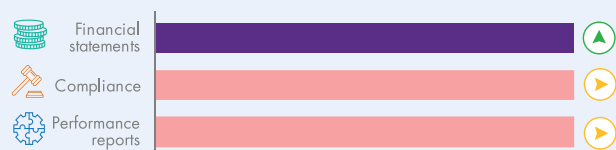


## Audit outcomes

Sapo had worked on improving the outcomes but was unfortunately qualified due to lack of controls to ensure that transactions were regularly recorded and reconciled for grant payouts



### Audit outcomes on three key areas



**Financial statements:** Qualified on trade and other receivables, other deposits (grants), and financial instruments and risk management

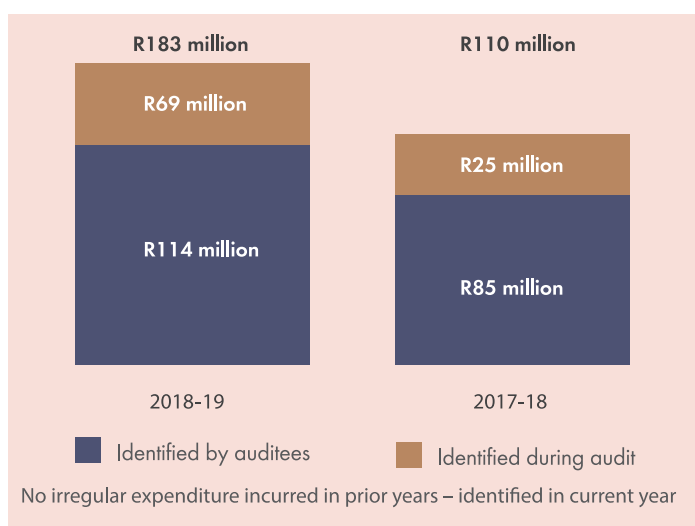
**Compliance:** Findings on quality of financial statements, revenue management, expenditure management, asset management, effecting consequences as well as procurement and contract management

**Performance reports:** Material findings on usefulness and reliability in current and previous year

Unqualified Qualified Disclaimed With no findings With findings



## Irregular expenditure



## Financial health

### Going concern status



Material uncertainty on going concern due to loss of R1,1 billion in 2017-18 and 2018-19. Sapo had a high cost base with employee costs accounting for 69% of their revenue, which contributed to constant operating losses. Trade and other payables increased to R1,6 billion from R1,4 billion in 2017-18.

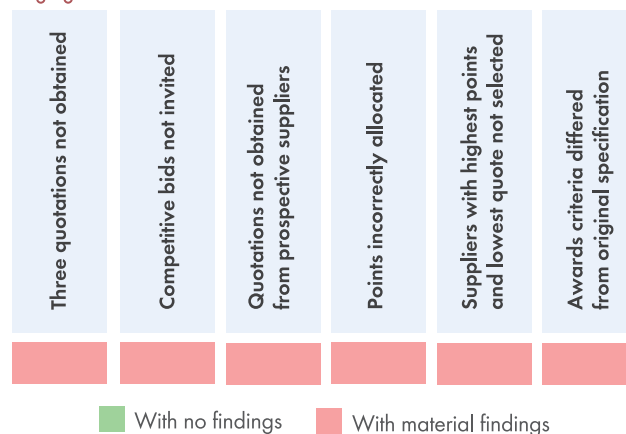
Sapo signed an agreement for grant payments with the South African Social Security Agency. National Treasury also approved funding for the universal service obligation / public service mandate amounting to R1,5 billion over the Medium-term Expenditure Framework period. During the 2018-19 mid-term budget adjustment, Sapo was further allocated R2,9 billion to fund future capital expenditure and operations.

- Good
- Of concern
- Intervention required

### Financial health indicators



## Findings on supply chain management



Sapo continued to have material findings on procurement, due to supply chain management staff lacking the necessary skills and competence to implement supply chain management policy and comply with necessary supply chain management requirements.



## Vacancies and stability

Vacancies at year-end	Accounting authority	No vacancies
	Chief executive officer*	Not vacant
	Chief financial officer**	Vacant

\* Chief executive officer resigned in August 2019

\*\* Acting chief financial officer was in place

Stability (average number of months in position)	Chief executive officer*	12
	Chief financial officer	Vacant



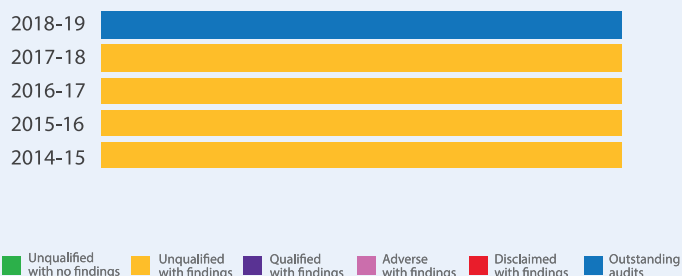


(Audited by AGSA)

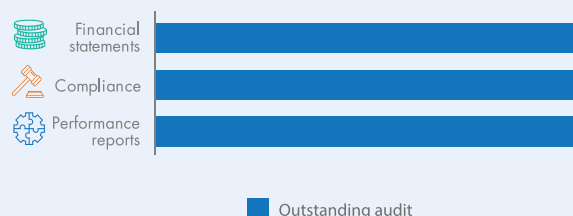


## Audit outcomes

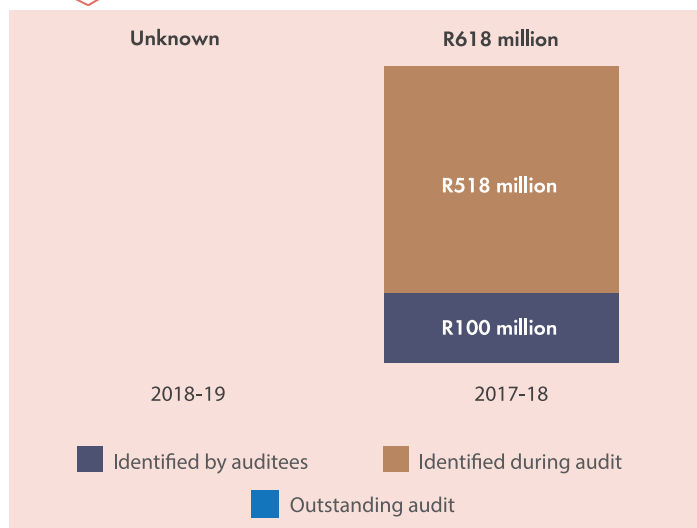
Outcome is outstanding since the audit report has not yet been signed



## Audit outcomes on three key areas

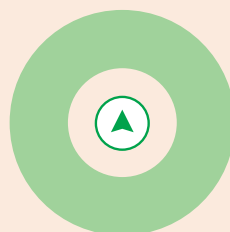


## Irregular expenditure



## Financial health

### Going concern status



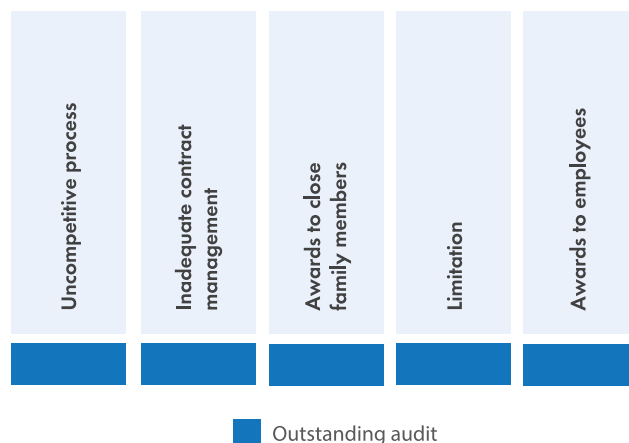
- Good
- Of concern
- Intervention required

### Financial health indicators

The audit is still outstanding and therefore we have not concluded our assessment of TCTA's going concern and financial health.

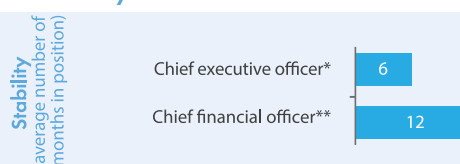


## Findings on supply chain management



## Vacancies and stability

Vacancies at year-end	Accounting authority	No vacancies
	Chief executive officer*	Vacant for more than 6 months
	Chief financial officer**	Vacant after financial year



\* Chief executive officer appointed in October 2018

\*\* Chief financial officer resigned in June 2019





# Air Traffic and Navigation Services (ATNS)

(Audited by audit firm)

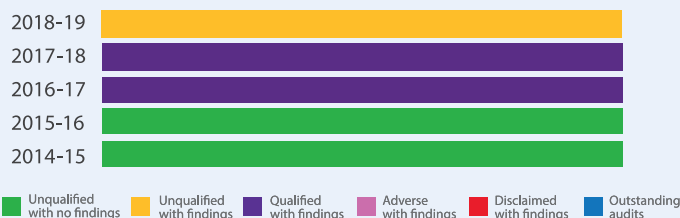


Overall improvement in audit outcome

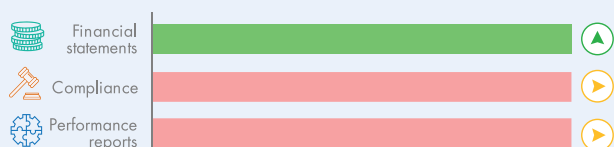


## Audit outcomes

Overall improvement compared to prior two years



## Audit outcomes on three key areas



**Financial statements:** Unqualified due to ATNS correcting the material misstatements identified

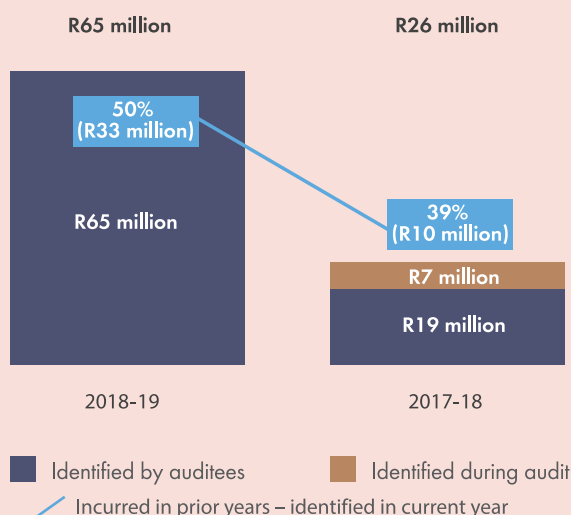
**Compliance:** Material non-compliance relating to quality of financial statements, procurement and contract management, effecting consequences as well as expenditure management

**Performance reports:** Material findings on reliability, as reported targets were not useful or supported by evidence

Unqualified (Green), Qualified (Purple), Disclaimed (Red), With no findings (Light Green), With findings (Pink)



## Irregular expenditure



## Financial health

### Going concern status

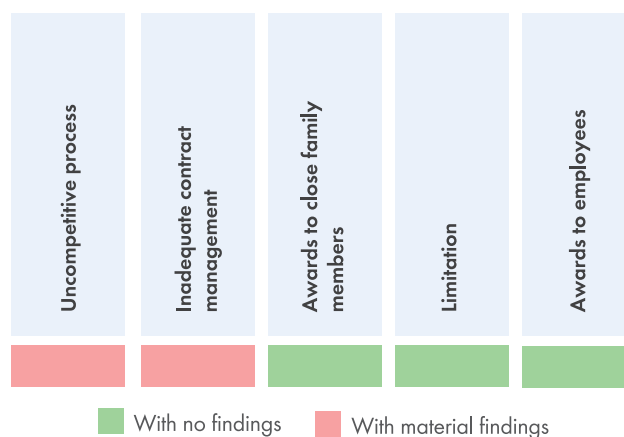


No material uncertainty on going concern evident

Good (Green), Of concern (Yellow), Intervention required (Pink)



## Findings on supply chain management



Lack of competitiveness in procurement of some goods, works and services. Contracts not monitored effectively, resulting in irregular expenditure. Root causes of non-compliance matters were slow response in implementing controls to monitor compliance with legislation, lack of controls to effectively monitor contracts as well as lack of implementation of consequences.



## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Vacant for more than 6 months
Chief financial officer	Vacant for more than 6 months

Stability (average number of months in position)

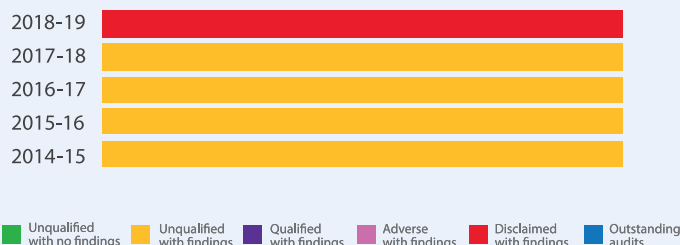
Chief executive officer	Vacant
Chief financial officer	Vacant





## Audit outcomes

Regressed to disclaimer due to material uncertainties that cast significant doubt on Alexkor's ability to continue as going concern



## Audit outcomes on three key areas



**Financial statements:** Disclaimed due to material limitations on use of going concern assumption in preparation of financial statements

**Compliance:** No material non-compliance

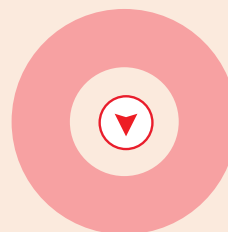
**Performance reports:** Material findings on usefulness relating to two of the five objectives audited

Legend: Unqualified (green), Qualified (purple), Disclaimed (red), With no findings (light green), With findings (pink).



## Financial health

## Going concern status

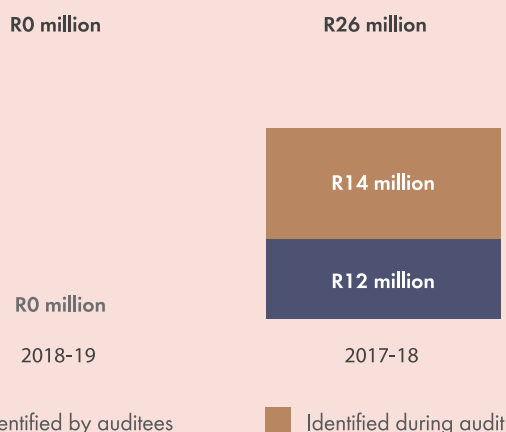


Material uncertainty on going concern due to liquidity issues. Alexkor had no other income-generating operations apart from its 51% investment in a pooling and sharing joint venture. Therefore, Alexkor is exposed to the financial challenges that face this venture. Furthermore, no financial support was received from shareholder. No turnaround strategy was provided.

Legend: Good (green), Of concern (yellow), Intervention required (red).



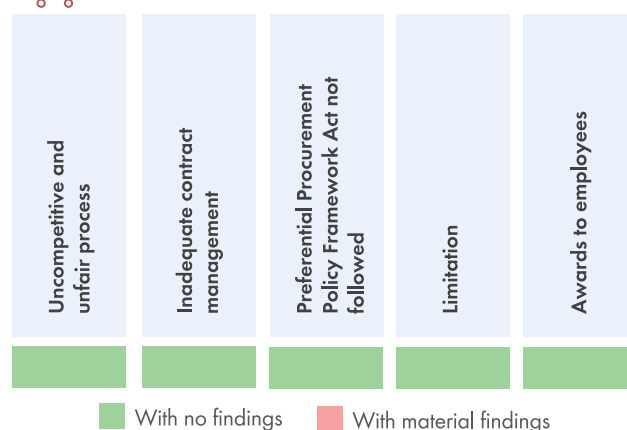
## Irregular expenditure



No irregular expenditure incurred in prior years – identified in current year



## Findings on supply chain management



Legend: With no findings (green), With material findings (red).

There were no findings on supply chain management as Alexkor did not have money to spend and awarded only two tenders and 16 quotations, which complied with relevant legislative requirements



## Vacancies and stability

Vacancies at year-end	Accounting authority	No vacancies
	Chief executive officer	Not vacant
	Chief financial officer	Not vacant

Stability (average number of months in position)	Chief executive officer	22
	Chief financial officer	21

Chief operations officer position was the only one vacant for more than 6 months





# Broadband Infraco (BBI)

(Audited by audit firm)

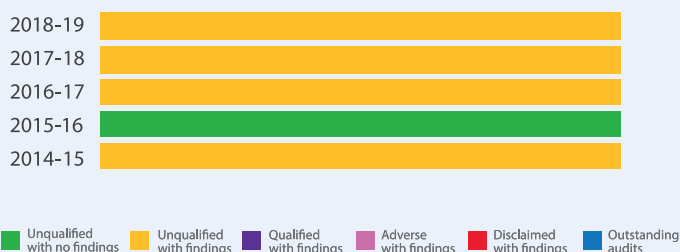


Overall stagnation in audit outcome

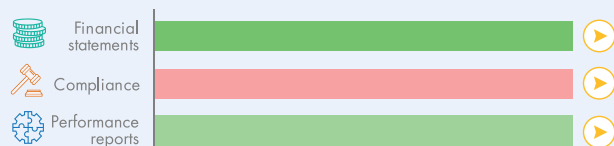


## Audit outcomes

### Unqualified with findings on compliance



### Audit outcomes on three key areas



**Financial statements:** Unqualified

**Compliance:** Findings on expenditure management as well as procurement and contract management

**Performance reports:** No findings

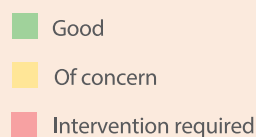


## Financial health

### Going concern status



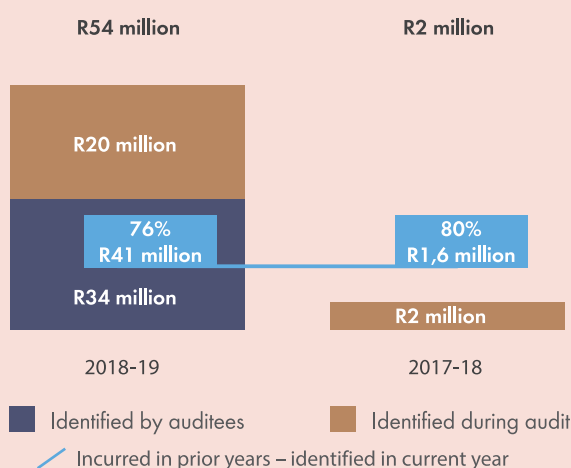
Material uncertainty on going concern due to loss of R113 million (2017-18: R127 million) and current liabilities exceeding current assets by R154 million at year-end (2017-18: R127 million). Trade and other payables increased to R85 million from R77 million in 2017-18.



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## Irregular expenditure



The significant increase in irregular expenditure was mainly caused by two instances where BBI used a supplier even though the contract had expired without being extended



## Findings on supply chain management



BBI continued to have material findings on procurement due to lack of proper procurement and contract management processes as well as inadequate action plans

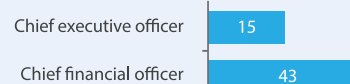


## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Not vacant
Chief financial officer	Not vacant

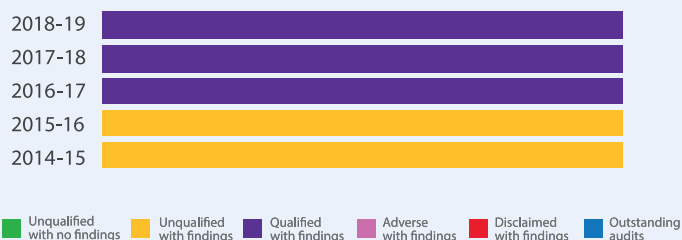
Stability (average number of months in position)



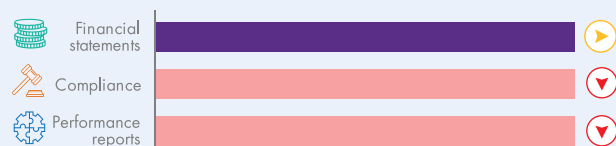


## Audit outcomes

Remained stagnant on qualified with findings



## Audit outcomes on three key areas



Material non-compliance with section 55(1)(b) of the PFMA (financial statements were not prepared in accordance with financial reporting framework) – financial statements received a qualified opinion

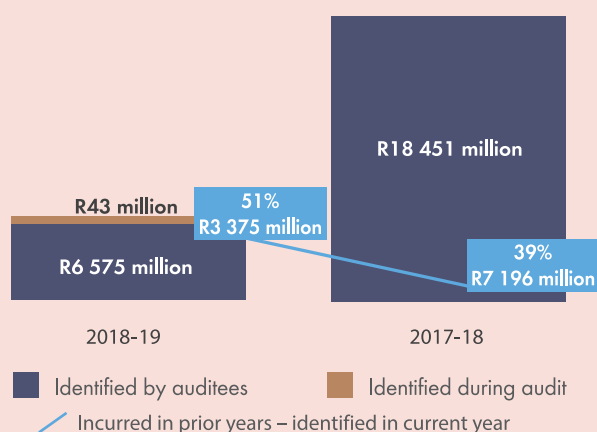


## Irregular expenditure



R6 618 million

R18 451 million



Full extent of irregular expenditure could not be confirmed as per our basis for qualified opinion



## Vacancies and stability

Vacancies at  
year-end

Accounting authority	No vacancies
Chief executive officer*	Not vacant
Chief financial officer	Not vacant

Stability  
(average number of  
months in position)

Chief executive officer	10
Chief financial officer	4

\*Chief executive officer resigned in May 2019

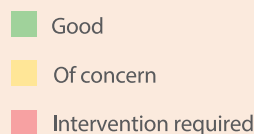


## Financial health

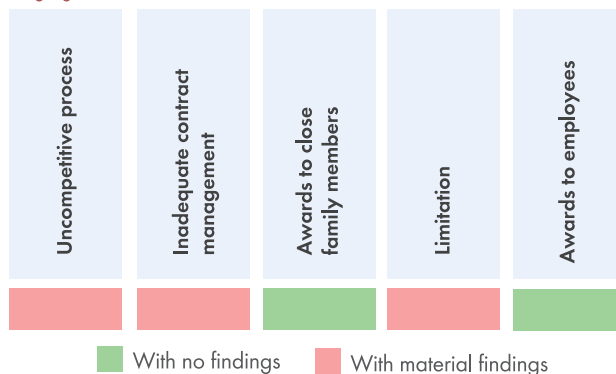
## Going concern status



Material uncertainty on going concern due to current and prior year losses, current liabilities exceeding current assets, deterioration in most of the financial indicators, impact of reduced generation performance, and debt-reliant liquidity situation



## Findings on supply chain management



Findings related to uncompetitive and unfair processes; non-compliance with Preferential Procurement Policy Framework Act and Preferential Procurement Regulations (local content and production); limitations; and Construction Industry Development Board requirements not met. The supply chain management environment was weak due to lack of proper oversight and monitoring by accounting authority, which subsequently resulted in a number of investigations, suspensions and transgressions as reported in the financial statements. This led to high irregular expenditure being reported in the financial statements although the completeness of the amount could not be confirmed.

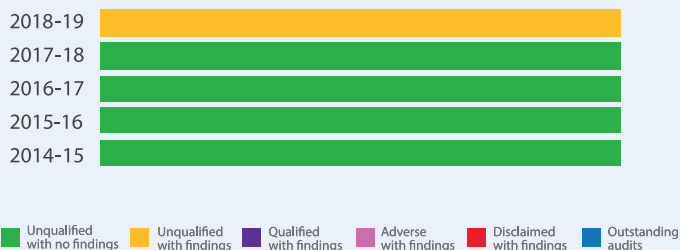


(Audited by audit firm)

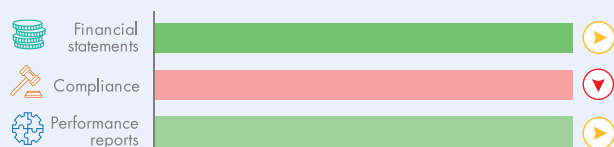


## Audit outcomes

### Regression due to one material non-compliance finding



### Audit outcomes on three key areas



Material non-compliance with section 55(1)(b) of the PFMA (financial statements were not prepared in accordance with financial reporting framework) – financial statements received an unqualified opinion after material adjustments to disclosure notes during the audit

Unqualified Qualified Disclaimed With no findings With findings



## Financial health

### Going concern status



No material uncertainty on going concern evident

Good  
Of concern  
Intervention required



## Irregular expenditure



R6 million

R1 million

R6 million

R1 million

2018-19

2017-18

Identified by auditees

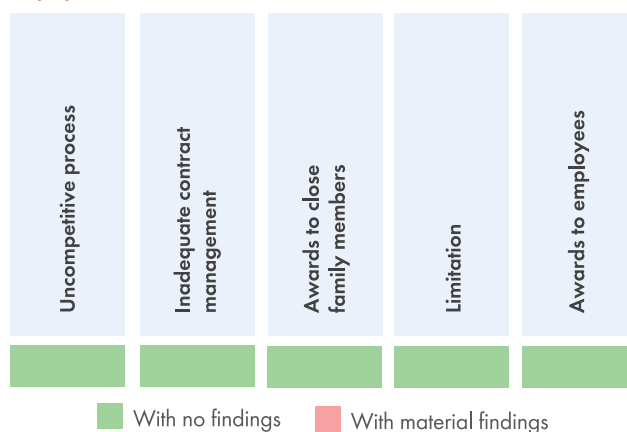
Identified during audit

No irregular expenditure incurred in prior years – identified in current year

Value of irregular expenditure was trivial and did not result in material supply chain management compliance findings



## Findings on supply chain management



## Vacancies and stability

Vacancies at year-end

Accounting authority	No vacancies
Chief executive officer	Not vacant
Chief financial officer	Not vacant

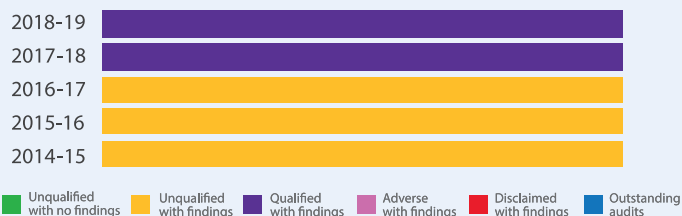
Stability (average number of months in position)



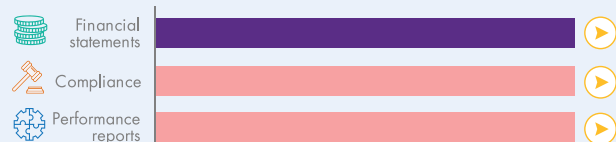


## Audit outcomes

Remained stagnant on qualified with findings on performance report and compliance due to root causes of qualifications not being addressed, resulting in qualification relating to completeness of irregular expenditure disclosure



## Audit outcomes on three key areas



**Financial statements:** Qualification on completeness of irregular expenditure note in financial statements: related to prior year qualification that remained unresolved as well as further instances of irregular expenditure identified by the auditors in 2018-19 that were not disclosed by management

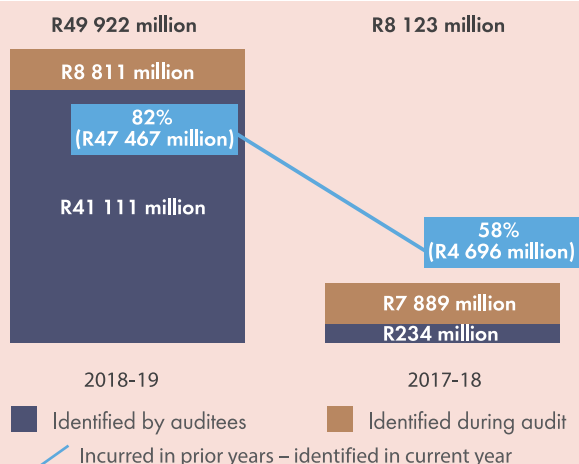
**Compliance:** Findings on expenditure management as well as procurement and contract management

**Performance reports:** Material findings on usefulness of performance indicators and targets; furthermore, a number of reported achievements were not reliable or could not be substantiated

Unqualified Qualified Disclaimed With no findings With findings



## Irregular expenditure



Full extent of irregular expenditure could not be confirmed as per our basis for qualified opinion



## Vacancies and stability

Vacancies at  
year-end

Accounting authority	No vacancies
Chief executive officer	Vacant for less than 6 months
Chief financial officer	Vacant for less than 6 months

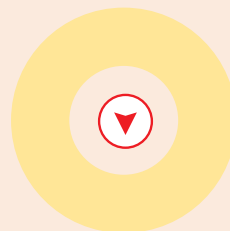
Stability  
(average number of  
months in position)

Acting chief executive officer	6
Acting chief financial officer	6



## Financial health

## Going concern status

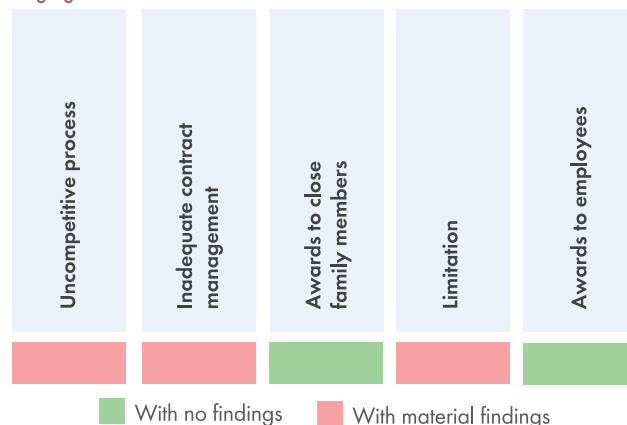


We emphasised going concern in current and previous financial year, due to breach of loan covenants by modification of audit opinion that triggers potential recall of loan facilities and insufficient resources to meet these in ordinary course of business

Good  
Of concern  
Intervention required



## Findings on supply chain management



Findings related to uncompetitive and unfair processes; non-compliance with Preferential Procurement Policy Framework Act and Preferential Procurement Regulations (local content and production); limitations; and Construction Industry Development Board requirements not met. The supply chain management environment was weak due to lack of proper oversight and monitoring by accounting authority, which subsequently resulted in a number of investigations, suspensions and transgressions as reported in the financial statements. This led to high irregular expenditure being reported in the financial statements although the completeness of the amount could not be confirmed.



## OVERSIGHT RESPONSIBILITY FOR STATE-OWNED ENTITIES

SOEs report to various oversight departments across government. These departments are responsible for providing strategic direction in terms of the overall mandate of the SOE and for monitoring the SOE's performance against predetermined objectives as required by the Public Finance Management Act. Additionally, the executive authority (which comprises the minister for the applicable oversight department and the shareholder of the SOE) annually agrees such predetermined objectives per the shareholder's compact signed between the accounting authority and the minister.

In some instances, **oversight departments did not have set programmes to govern and measure performance** against set targets in their annual performance plans to provide strategic direction to the SOEs in their portfolio. As a best practice, oversight departments (for example the ones listed in the table below) measure their performance against such targets. This should be used as a benchmark by those oversight departments that do not specifically measure the performance of their SOEs.

	National Treasury	Defence	Telecommunications and Postal Services	Water and Sanitation	Communications	Public Enterprises
SOEs in portfolio	Land and Agricultural Development Bank of South Africa	Armsscor	Broadband Infraco South African Post Office	Trans-Caledon Tunnel Authority	South African Broadcasting Corporation	Alexkor Denel Eskom South African Airways South African Express Airways South African Forestry Company Transnet

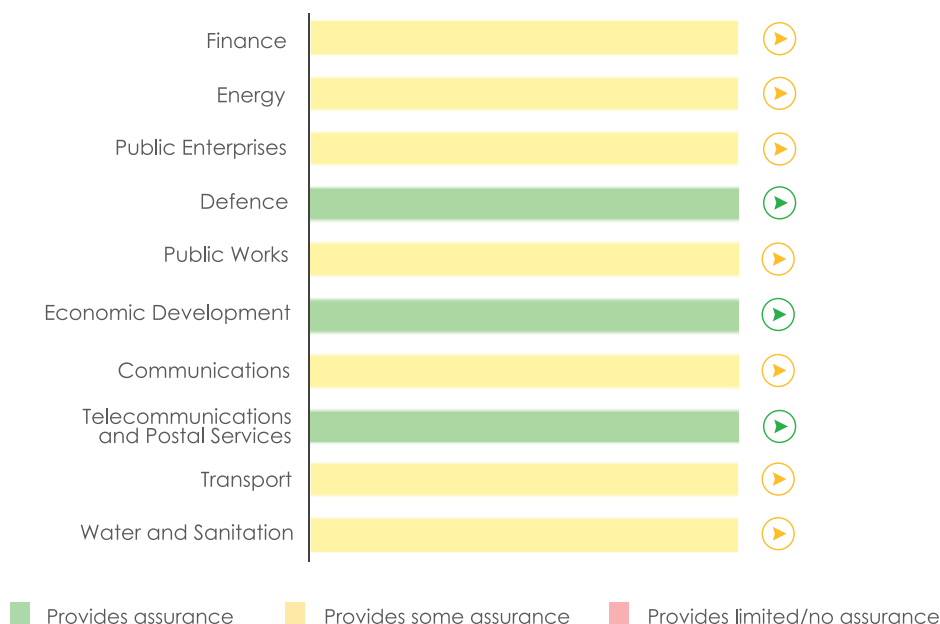
Executive authorities should provide assurance in line with the legislative requirements provided in the Public Finance Management Act and the Companies Act. The executive authority is expected to steer the SOE on its path to implementing the accountability wheel (as explained in section 2) as follows:

- Provide a clear and timeous shareholder's compact (**PLAN**).
- Set clear expectations for the accounting authority to comply with based on approval of policies (**DO**).
- Monitor quarterly performance relating to predetermined objectives and compliance with legislation (**CHECK**).
- Take appropriate measures to institute consequences against the accounting authority when periodic measures are not in line with planned policies (**ACT**).

- Table the annual financial and performance results in Parliament in terms of legislation to enable oversight bodies and other users to hold the executive accountable (**ACT**).

As reflected in the graphic on the following page, we assessed that the executive authorities of Defence, Economic Development, and Telecommunications and Postal Services provided adequate assurance based on the considerations per the accountability wheel. However, the executive authorities of Finance (National Treasury), Communications, Energy, Transport, Water and Sanitation, Public Works, and Public Enterprises provided only some assurance, mainly due to a lack of a timeous plan agreed with the accounting authorities to enable accountability for the performance of SOEs during the year. The annual financial statements and performance results of some of the SOEs in the public enterprises and energy portfolios were tabled very late or have not been tabled in Parliament.





## CONCLUSION

The **root causes of the regression** in the overall audit outcomes of SOEs were weak internal control environments (**PLAN**), instability in appointed senior management positions (**DO**), and a lack of implemented action plans (**DO**) to address previously reported audit findings. These matters, together with inadequate compliance monitoring (**CHECK**), resulted from management and those charged with governance being preoccupied with resolving the financial viability challenges encountered by the SOEs. In addition, consequences were not properly used (**ACT**) as a deterrent for those found to contravene legislation, painting a similar picture as in the previous year.

This section started off by acknowledging the importance of SOEs in the South African context. This principle was recognised in 2014 when the previous head of state commissioned a presidential review committee on SOEs. The committee's suggested principles remain at the core of steering our SOEs in the right direction. Since the committee's report had

been tabled, positive developments have transpired, such as the recommendations of the committee being considered during the development of the country's National Development Plan.

Some of the principles that have not been implemented, such as a centralised shareholder ownership framework for all SOEs, need to be prioritised by the executive. This should ideally include matters such as clarity in SOE legislative requirements; a clear split between SOEs' social and commercial mandate; financial viability standards; remuneration principles; and separating government's role as owner, policymaker, regulator and implementer in the respective industries in which the SOEs operate.

We echo our president's recognition of the important role that SOEs play in the South African economy. This section therefore aims to provide those charged with governance with relevant insights and recommendations so that they can act to turn around SOEs for the benefit of all citizens.



We believe the following can serve as a recipe to get our SOEs back on track:

**S**tabilise leadership

**O**perationalise action plans

**E**valuate periodically