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Auditor-General reports steady progress, but calls on government to "accelerate improvements in accountability"

PRETORIA – The Auditor-General (AG), Tsakani Maluleke, today tabled in Parliament the 2020-21 Public Finance Management Act (PFMA) audit outcomes general report. The report is a statutory and annual requirement for the AG, to report on the outcomes of the audits for the financial and performance year, which ended 31 March 2021.

The overall outcomes reflect "incremental improvement" in the national and provincial government audits, with an increase in the number of clean audits. However, the report also records low levels of accountability among accounting officers and accounting authorities.

In this regard, the AG continues to call for higher levels of accountability, which are necessary if the public sector is to implement the changes required to ensure that public finances are spent efficiently in the delivery of services that benefit citizens. This is reflected in the theme under which the report is tabled – ***accelerate improvements in accountability***.

The audit outcomes of national and provincial government and their entities, though improving, continue to show slow progress in the journey towards wholesale good governance. This is particularly concerning for two areas that are still lagging behind in this improvement trend – state-owned enterprises and the key service delivery departments of health, education, housing and public works, which have the greatest impact on the lives of citizens and government's financial health.

Poor financial and performance management in the key service delivery departments means that citizens are denied critical services that can help sustain and improve their lives.

"Service delivery is of key concern for all South Africans, especially in a period where limited resources are available to respond to the service delivery needs, which have increased due to the outbreak of the covid-19 pandemic," says Maluleke. "Therefore, oversight structures need to pay particular attention to service delivery departments, and all role-players must be vigilant and exercise their duties with diligence."

Audit results moving towards clean audits

In the 2020-21 audit cycle, the AGSA audited 679 departments and public entities, and in this report we focus on the results of 425 audits. There are 34 incomplete audits, which require attention and decisive action from oversight and executive authorities.

In the third year of the current administration, improvements in the audit outcomes of national and provincial government were recorded. These can be attributed to the following:

- Accounting officers and authorities and senior management were committed to, and got directly involved in, ensuring that internal control processes were improved and the audit office's recommendations were implemented. There was also notable stability in these key positions.
- Internal controls were improved – this includes the consistent implementation of preventative controls.
- Accounting officers and authorities, executive authorities, internal audit and audit committees provided oversight, monitoring and assurance.

In response to the outcomes, AG Maluleke says, "If all auditees were to consistently implement these basics, the drive towards overall good governance in the public sector would be realised sooner and be sustained in the future."

The AGSA noted that the number of clean audits increases every year "due to significant effort and commitment by the leadership, officials and governance structures" of the auditees that produced the desired audit outcomes.

There are 115 auditees (48 departments and 67 public entities) that obtained a clean audit outcome, compared to 109 in the previous year. Together, these auditees are responsible for 19% of the R1,9 trillion expenditure budget managed by national and provincial government.

Maluleke acknowledges that at least 31 auditees are close to obtaining a clean audit and require sustained effort to reach this goal, and says that her office is encouraged that 61 auditees have managed to retain their clean audit status since the first year of the current administration.

"The improvements in audit outcomes are a clear indication that some auditees are listening to our messages, heeding our call and implementing the necessary interventions to realise improvements. While we are yet to see the progressive and sustainable improvements required to realise an overall change in outcomes, we note and acknowledge the efforts of the many accounting officers and authorities that seek to instil a culture of good governance, accountability and discipline in the system," she says.

Maluleke explains that while a clean audit is not always an indicator of good service delivery, "auditees that have the controls and systems in place to plan, measure, monitor and account for their finances and performance, and to comply with the rules, often have a solid foundation for service delivery that will benefit the citizens of South Africa. Therefore, all these efforts are a step in the right direction and must be sustained to ultimately realise overall improvement in the performance of public institutions".

Incomplete audits

Departments and entities are required to submit their financial statements for audit by 31 May each year, and AGSA conducts its audits over a two-month period following this submission. The audit reports are then included in the departments' and entities' annual reports, and presented to Parliament and provincial legislatures as part of the accountability process. The AGSA sometimes encounters delays in the completion of audits for various reasons.

In the year under review, there are 34 audits that have not been finalised due to: outstanding financial statements (17), financial statements being submitted late (4) and delays in audit process (13). The details are further elaborated in the report.

Auditees that fail to present financial statements and performance reports for auditing, as required by legislation, effectively undermine the overall efforts made by many role-players to improve transparency and accountability.

Poor-quality financial statements submitted

While submitting financial statements is the crucial first step for enabling accountability and transparency, auditees must also ensure that their financial statements are credible. Regrettably, more than half of auditees submitted poor-quality financial statements. This means that if the AGSA had not identified misstatements in these financial statements and given the auditees an opportunity to correct them, only 182 auditees (43%) would have received unqualified audit opinions, compared to the 302 (71%) that ultimately received this outcome. The AG calls on auditees to invest in personnel who have the necessary skills and competencies to manage their finances and to put adequate controls in place.

State-owned enterprises (SOEs)

The audit outcomes of SOEs have regressed due to weak controls and disciplines over financial and performance management, as well as compliance. The report sets out the deteriorating financial health of SOEs, which has increased the financial burden on government, through bailouts and guarantees. These concerns spill over into the ability of SOEs to fulfil their mandates and directly affects the South African economy and, ultimately, the lived experiences of South African citizens.

There are seven (7) SOE audits outstanding for this year that had material uncertainties on their ability to continue as a going concern in previous years – Alexkor, the Land and Agricultural Development Bank (Land Bank), the Independent Development Trust, the South African Post Office, South African Airways, South African Express Airways and Denel.

"We are particularly concerned about a growing trend of late or non-submission of financial statements, and thus performance reports and annual reports, specifically at SOEs. This affects oversight's ability to hold SOEs accountable and implement consequence management where necessary," says Maluleke.

According to the *National Planning Commission position paper on the contribution of SOEs to vision 2030* (2020: 8), SOEs' "aim and intention is to provide core economic infrastructure and services efficiently; to drive economic development and trade; to drive down the cost of doing business; to lead on spatial and industrial transformation; and to provide minimum basic goods and services like water and sanitation, energy and transport".

Therefore, it is important to for the executive and oversight to pay particular attention to addressing the deficiencies at SOEs and ensure that appropriate interventions are urgently implemented to enable them to effectively fulfil their mandates. Given the urgent challenges of economic hardship, jobs and inequality in our society, this cannot be overstated.

Disclaimed audit opinions

Thirteen (13) public entities received disclaimed opinions in 2020-21. This is the worst audit outcome an auditee can get, as it means that they could not provide auditors with evidence for most of the important amounts and critical disclosures in their financial statements, which significantly undermines the reliance that users of financial statements can place on the information presented.

The entities that received this undesirable opinion are:

- Necsa
- Pelchem
- Gauteng Housing Fund
- Compensation Fund
- National Skills Fund
- four technical and vocational education and training (TVET) colleges(Central Johannesburg, South West Gauteng, Tshwane North and Taletso)
- Golden Leopard resorts (a public entity in the North-West) and its subsidiary GL resorts)
- both the Free State and North West development corporations.

All 13 public entities had also received disclaimed opinions in 2019-20.

Another nine public entities that had previously received disclaimed audit outcomes had either not submitted their financial statements for auditing by the cut-off date for inclusion in this report, or had submitted them so late that the audit was still in progress. These entities include:

- Passenger Rail Agency of South Africa (Prasa)
- Independent Development Trust
- Denel

Financial health of departments

Unauthorised expenditure

Unauthorised expenditure remains high at a total R3,21 billion, mostly due to overspending of the budget. Legal claims against government departments, particularly in the health sector, further reduce the limited funds available for intended programmes.

The AG stresses that, especially in such challenging circumstances, good financial management should be reinforced to ensure that the limited funds available are spent wisely and within budget.

The key service delivery departments (health, education and public works) have the poorest financial health of all, which affects their ability to deliver services to citizens. In total, these departments incurred 90% of all unauthorised expenditure and their deficits amounted to R15,65 billion. Five provincial health departments had deficits totalling R6,2 billion.

The provincial health departments paid out R1,76 billion for medical negligence claims, while the estimated settlement value of unpaid claims at year-end was R124,15 billion (75% of the total claims against the state). Seven provincial health departments had unpaid claims at year-end that exceeded their entire operational budget for the next year.

The AG cautions that the growing trend of departments using the next year's budget to pay the current year's expenses and claims adversely affected their ability to pay creditors on time, and continues to have a negative impact on service delivery.

Fruitless and wasteful expenditure

Fruitless and wasteful expenditure is defined in the Public Finance Management Act as expenditure which was made in vain and would have been avoided had reasonable care been exercised.

It is also a good indicator of the discipline with which the public purse is managed. The report indicates that fruitless and wasteful expenditure remains high, with 224 auditees losing a combined R1,72 billion to fruitless and wasteful expenditure in the current year.

The report reveals that key service delivery departments and SOEs were, once again, the main contributors, wasting a combined R0,90 billion (52%). At a time when there are limited funds available, the state cannot afford further leakages, and urgent action is required from accounting officers, the executive and oversight.

Irregular expenditure increased

Irregular expenditure reported in the financial statements increased to R166,85 billion, from R109,82 billion in the previous year. Such expenditure, especially as it relates to procurement, is an indication that auditees do not follow supply chain laws and regulations when making decisions.

Performance information

The national audit office is required to provide assurance that the financial statements of auditees are free from material misstatements, report on the usefulness and reliability of the information in the annual performance reports, report on material non-compliance with relevant key legislation, and identify key internal control deficiencies that should be addressed.

The audit office does not provide a full account of service delivery, as its audit mandate does not extend to this. While the office will occasionally conduct performance audits that evaluate the qualitative areas of delivery, these specialised audits are not conducted every year.

In this audit cycle, the AGSA conducted performance audits on infrastructure delivery, which is critical for service delivery. The focus was on the key service delivery departments of health, education and human settlements.

Infrastructure

As the custodian of government's immovable properties, the public works sector has the mandate to provide user departments with the necessary infrastructure to deliver services to the public. The report reflects on significantly delayed infrastructure projects, as well as poor and unfit properties that are being used and that have been closed, thereby affecting service delivery. Additionally, mismanagement of lease contracts is resulting in a loss of funds that could be used to fulfil key targets supporting the department's mandate.

It is thus critical for the sector to prioritise key initiatives that directly support its mandate, such as facility management and on-time completion of infrastructure projects. It should also curb the financial losses and irregular expenditure arising from mismanaged leases so that these funds can be used to maintain properties and enable infrastructure projects to be completed on time. This will also ensure that key service delivery departments such as education, health, and security and safety services are not negatively affected by significantly delayed projects, or by poor and unfit properties.

The health, education and human settlements sectors received a combined R34,32 billion in grant funding for infrastructure projects to create sustainable human settlements and build healthcare infrastructure, as well as build and/or upgrade schools.

However, our findings reveal that reported deficiencies continue unattended, resulting in delayed project completion; increased project cost and financial losses; defects in build quality; and completed infrastructure not being commissioned or being under-utilised. The impact is that the much-needed services are not delivered and citizens are left wanting.

"We call upon the accounting officers to pay particular attention to strengthening the controls that support the effective and efficient implementation of infrastructure projects, as they have a direct impact on the lived experiences of citizens," says Maluleke.

Information technology (IT)

The report identifies significant control weaknesses in government's information systems, and exposes the lack of urgency to address these challenges, resulting in continued system vulnerabilities, project failures and financial loss. Government continues to spend money on new and advanced systems to streamline its processes. However, due to significant system weaknesses, the auditors could not rely on the transactions and data processed by most of these systems. The systems are also vulnerable to misuse, abuse and fraud.

Through our audits this year, we found that auditees spent a total of R1,7 billion on system implementation projects that did not meet business expectations, and paid R46 million for software licences they did not need.

"Poor management of IT systems makes government institutions inefficient, which compromises service delivery, says Maluleke.

Material irregularity implementation results

In 2019, the Public Audit Act was amended and gave the AG enhanced powers to hold auditees accountable for their failure to address recommendations reported on during audit. The amendment introduced the concept of material irregularities.

This refers to any non-compliance with, or contravention of, legislation, or fraud, theft or a breach of a fiduciary duty identified during an audit performed under the Public Audit Act that resulted in, or is likely to result in, a material financial loss, the misuse or loss of a material public resource, or substantial harm to a public sector institution or the general public.

The material irregularity process has been implemented since 2019. In this report on national and provincial government, there are 121 material irregularities at various stages in the process of being addressed, with a combined estimated financial loss of R11,9 billion.

The material irregularities relate to non-compliance with procurement processes, payment of goods and services not received, revenue not billed, inefficient use of resources and suspected fraud resulting in financial loss.

The report notes that accounting officers are acting on the identified material irregularities and we are regularly monitoring them to ensure accountability. The audit office has made progress in implementing the material irregularity process, and is confident that with clear and deliberate implementation, it will contribute to improved accountability.

The material irregularity process is complementary and supports consequence management where there has been wrongdoing that is identified through an audit. The process promotes better accountability, which, in turn, results in the protection of valuable public resources and enhancement of the performance of that public institutions.

First remedial actions issued

"We have been clear from the start that we will not hesitate to implement our expanded powers if accounting officers and authorities do not deal with material irregularities with the required urgency. In cases where accountability has failed, we have responded accordingly. In this regard we have taken this matter a notch further, by issuing the first-ever remedial action to enforce accountability," says Maluleke.

In 2021, the AG issued the first four remedial actions – to the accounting officers and authorities of Prasa (one remedial action), the Department of Defence (one) and the Free State Department of Human Settlements (two). The remedial action to the two departments included a directive to deal with the financial loss by the stipulated date, which, if not implemented, could result in a certificate of debt being issued.

"We are encouraged by the response of accounting officers in general to deal with identified material irregularities. This is the type of accountability that must be institutionalised, where accounting officers decisively and consistently act on audit findings and other weaknesses beyond those flagged as material Irregularities," says Maluleke.

Provincial audit outcomes

The AG's report acknowledges the gradual improvements in most of the provinces and urges "provincial leadership and legislatures to focus on implementing sustainable solutions at provincial departments and public entities to improve the audit outcomes and delivery in the provinces".

Details are available in the report.

Conclusion

Maluleke says the improvements in audit outcomes and year-on-year increases in clean audits are a feather in the cap of this administration, adding that "some auditees are close to achieving a clean audit status and just need to get over the very last hurdles. We continue to call upon the leadership to accelerate and sustain the improvements in accountability."

End.

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Media note: The *consolidated general report on the PFMA national and provincial government audit outcomes* will be available on www.agsa.co.za.

Scan the QR code to access the full PFMA general report: