AUDITOR-GENERAL SOUTH AFRICA

MEDIA RELEASE

31 March 2021

Auditor-General calls on government leaders to ensure 'sustainable' audit outcomes

PRETORIA – Auditor-General (AG) Tsakani Maluleke today reported "signs of improvement" in the national and provincial government audits, and strongly urged government leaders to ensure "progressive and sustainable improvements" in their outcomes.

The Auditor-General also reiterated the theme of the 2018-19 report, ***act now on accountability***, out of concern that little progress was made in addressing concerns raised in the previous year. The concerns were also highlighted in the two special reports tabled in 2020 on the financial management of government's covid-19 initiatives and related to 1) sustainable solutions required to prevent accountability failures; 2) ensuring consequences for accountability failures; 3) prioritising improving financial management of auditees; 4) taking opportunities for progressive and sustainable change.

Releasing the 2019-20 general report (GR) for national and provincial government and their entities – her first GR since taking office as AG last December – Maluleke says although there are signs of improvement at some auditees, her office "cannot yet see the progressive and sustainable improvements required to prevent accountability failures and deal with them appropriately and consistently across national and provincial government".

A continued call to act on accountability

The AG says her office's message for the 2019-20 report is tabled under the theme a ***continued call to act on accountability***, which is consistent with the previous year and says:

- Although the improvements in audit outcomes are encouraging, **the sustainable solutions required to prevent accountability failures** are not yet in place, and will require investments from all levels of government.
- Oversight, executive authorities and coordinating departments should pay **specific attention to state-owned entities, struggling public entities and the key service delivery departments** such as health and education. The inability of these auditees to sustain their operations and continue to deliver services will – and is having - a significant impact on government finances and the lives of citizens.
- The importance of **financial management disciplines** in this time cannot be underemphasised – every official must do their part to ensure public money is protected and there is transparency and accountability for the way it is managed.
- **Preventing leakages and recovering money** that have been lost will need to be a key priority of all accounting officers and authorities in this time when much must be done with very limited and continually decreasing financial resources.
- If **consequences for accountability failures** are required, these must be effected swiftly, bravely and consistently.

We believe that if sufficient attention is directed at these, we will realise the improvements required and will contribute to the success of our auditees.

Impact of covid-19 in the 2019-20 audit process

The pandemic and the lockdown affected the reporting and audit processes for the 2019-20 financial year, resulting in the delayed release of the report.

The national audit office had to adapt to working remotely and technology has been of great value and we found new ways of working in partnership with our auditees. In this time, we conducted both 2019-20 audits with real time audits of the covid-19 initiatives conducted from March 2020. We also tabled two special reports on the financial management of government's covid-19 initiatives.

A. Audit outcomes at a glance

Key features of the audit outcomes

Overall, **audit outcomes improved** with 66 auditees improving and 35 regressing. We observed that the main reasons for improvements were:

- Vacant key management positions were filled – most notably those of accounting officers and chief financial officers. We have often observed that stability in key positions has been a driver of improving poor audit outcomes and maintaining good audit outcomes.
- Accounting officers and senior management were committed and got directly involved to ensure improvements in internal control processes and implement our recommendations
- Improvements in the internal controls – including implementation of preventative controls

The report reveals the following key features of the audit results:

- There are 111 (26%) auditees that managed to produce quality financial statements and performance reports to comply with key legislation, thereby receiving a clean audit. This is a slight improvement from the 98 (23%) in the previous year. These auditees represent 17% of the expenditure budget of R1,7 trillion at national and provincial government.
- Countrywide, 74% of the auditees received unqualified audit opinions on their financial statements, a slight improvement from 71% in the previous year. The number of auditees that submitted quality financial statements increased – 49% of

the auditees could give us financial statements without misstatements, which is still very low.

- The quality of performance reporting showed an improvement in 2019-20, with 71% of the auditees now publishing credible reports compared to 60% in the previous year. The quality of the performance reports submitted for auditing remained poor (with only 39% submitting good-quality reports). Even after auditees corrected the misstatements identified by the auditors in the performance reports, the AGSA reported material findings on 29% of the performance reports.

- Overall, 69% of the auditees materially did not comply with legislation, which was 73% in the previous year.

- Compliance with supply chain management legislation slightly improved from the previous year. It remains concerning that only 36% of the auditees are fully complying. This is in spite of all the reporting we have done in this area, the red flags we have raised, and the many recommendations we have made. Uncompetitive and unfair procurement processes and inadequate contract management remain common.

Irregular expenditure decreases

- **Irregular expenditure decreased to R54,34 billion** from the R66,90 billion in the previous year. It includes the irregular expenditure (R7,71 billion) of those auditees of which the audits were completed after the cut-off date for this report (30 November) as well as the unaudited amounts disclosed in the financial statements of the auditees whose audits were still outstanding by the date of this report.

- The AG says the amount could however be higher, **as 31%** of the auditees were qualified because the amount disclosed was incomplete and/or disclosed that they had incurred irregular expenditure but that the full amount was not known. If the full irregular expenditure was disclosed there would not have been a decrease from the previous year.

- In addition, the AGSA could not audit R2,08 billion worth of contracts due to missing or incomplete information.

- Maluleke says that auditees have a poor track record when it comes to dealing with irregular expenditure and ensuring accountability. The year-end balance of irregular expenditure that had accumulated over many years and has not yet been dealt with stood at R262.03 billion.

Internal controls

The report reveals widespread weaknesses in the basic internal controls at a number of auditees. Among the lapses that impacted the results under review, the report highlights the following:

- The action plans of the accounting officers or authority to proactively address the root causes of audit findings from the previous year – the audit office found effective implementation of plans at only 34% of our auditees.

- Proper record keeping remained an area of weakness – only 42% of auditees had good controls.

- Auditors again did not find proper processes for in-year and year-end reporting – only 24% had good processes. This applied to financial matters, performance against targets and monitoring of compliance.

- The review and monitoring of compliance with legislation was again at a low level – only 25% had good controls to ensure compliance.

- Information technology (IT) systems controls also stand out as an area where the controls were particularly poor – only 8% of the auditees had good IT general controls.

Maluleke cautions that these are the controls that are key in preventing accountability failures; however, the audit indicates that "necessary investment has not yet been made in prevention".

B. Financial management

In the environment of economic upheavals when departments, state-owned entities and public entities need to do more with less and where the demand from the public for service delivery and accountability are increasing. Maluleke cautious that "accounting officers and authorities should do everything in their power to get the most value from every rand spent and manage every aspect of their finances with diligence and care."

Credible financial statements are crucial to enable accountability and transparency. The financial statements tell the story of how well an auditee is managed - how it spends its money, where its revenue comes from, its assets and the state of those assets, how much it owes creditors, how much is owed to the auditee, and whether it is expected that the money owed will be received. It also provides crucial information on how the budget was adhered to, the unauthorised, irregular as well as fruitless and wasteful expenditure incurred plus the overall financial position of the auditee – whether its operations are financially sustainable.

Maluleke says her office is concerned about the 21 auditees that received disclaimed or adverse opinions on their financial statements. She further says we could not analyse the financial health of these auditees, who are responsible for 2% of the expenditure budget.

Maluleke expressed concern that state-owned entities are in serious financial difficulty and did not submit financial statements for auditing. These include:

- South African Airways and LMT Products (a subsidiary of Denel) which are under business rescue
- SA Express is under provisional liquidation.

For most of the South African Airways group we have not seen financial statements for three years.

In addition, many state-owned entities disclosed uncertainty in their financial statements whether they will be able to continue as a going concern and they include:

- Petroleum Oil and Gas Corporation,
- South African Broadcasting Corporation,
- Denel and three subsidiaries (Densure, Denel Aerostructures and Denel Vehicle Systems),
- Independent Development Trust,
- Land and Agricultural Bank of South Africa,
- Pelchem and;
- South African Nuclear Energy Corporation
- Eskom

Financial Health of departments

Maluleke said the financial health of a number of departments continue to be alarming, especially the provincial departments of health and education. She called on accounting officers and executive leadership to pay serious attention in this area.

Unauthorised expenditure

Unauthorised expenditure which is as a result of overspending of the budget, increased from R1,65 billion to R18,12 billion – of which R15,13 billion was as a result of the early payment of the April 2020 social grants in response to the covid-19 lockdown measures.

Over 60% of the departments had insufficient funds to settle all liabilities that existed at year-end if the unpaid expenses (totalling R22,78 billion) were also taken into account. At total of 27 departments will have to use more than 10% of their 2020-21 operational budgets.

At year-end, 87% of the departments had claims against them, totalling R147,12 billion. Claims are made against departments through litigation for compensation as a result of a loss caused by the department – the most common claims are medical negligence claims against provincial health departments- totalling R105,8 billion.

There are also key public entities which are similarly under financial pressure. A total deficit of R64,95 billion was incurred by the 29% of public entities whose expenditure exceeded their revenue – 92% of the total deficit related to the Road Accident Fund.

There were 21 public entities that disclosed uncertainty about whether they will be able to continue as a going concern. They include:

- Road Accident Fund,
- South African National Roads Agency,
- Property Management Trading Entity and a number of provincial public entities.

The financial statements of 17 public entities were not reliable enough for financial analysis – these included the Passenger Rail Agency of South Africa, seven TVET colleges and four provincial entities in the North West.

Fruitless and wasteful expenditure

Fruitless and wasteful expenditure is money that is lost to the state or that could be permanently lost if not recovered. It is also a good indicator of the financial management of the public purse. Government cannot afford to lose money because of poor decision-making, neglect or inefficiencies. However, Maluleke's report indicates that fruitless and wasteful expenditure remains high.

In the current year, 231 auditees lost R2,39 billion in fruitless and wasteful expenditure. Over the last three years, R7.44 billion of government expenditure was fruitless and wasteful.

C. Material irregularity implementation results

Maluleke said the Public Audit Act amendment provide her office with the mandate to report on material irregularities detected during our audits and take further actions if accounting officers and authorities do not appropriately deal with such reported material irregularities.

We can refer the matter to a public body to investigate or include recommendations in the audit report on what should be done to address the matter. The amendments further give us the power to take binding remedial action if our recommendations are not implemented and, in certain circumstances, we can recover the money lost from accounting officers or authorities that do not implement the remedial actions.

Maluleke elaborates that "the amendments are not punitive, but intended to strengthen accountability mechanisms. By reporting material irregularities, we support accounting officers and authorities by bringing to their attention the irregularities that could have a significant impact on finances, resources and service delivery, while also empowering them to take the appropriate steps timeously in terms of legislation."

This will lessen the adverse effect of such irregularities on auditees, set the right tone for accountability, highlight the need for consequences, and encourage a behavioural change at the highest levels. As we report the material irregularities in the audit report, we also enable public accounts and portfolio committees to perform their oversight function – focusing on the most material matters affecting auditees.

Maluleke also emphasised that the "regulations have been shaped in a manner that supports the process of fair, transparent and legally sound administrative justice, by providing an opportunity to the accounting officer or authority to take the actions required to deal with the material irregularities."

Material Irregularities identified

"By 28 February 2021, we had notified the accounting officers and authorities of the selected auditees of 75 material irregularities. They all related to non-compliance with legislation that resulted in a material financial loss. The estimated financial loss associated with these material irregularities is R6,9 billion" Maluleke further said.

45 of these material irregularities have been included in the audit reports and in the general report to enable monitoring and oversight. The remainder will be reported in the 2020-21 audit reports.

There were also a high number of matters being considered which were identified during our audit of covid-19 expenditure and are in the key areas such as procurement, expenditure management, revenue management and resource management.

Maluleke further said "these are not complex matters, but the basic disciplines and processes that should be in place at auditees – procure at the best price, pay only for what was received, make payments on time, recover the revenue owed to the state, safeguard assets and make use of the resources of the state in the most effective and efficient manner ensuring that value is derived from the money spent. Good preventative controls would have made all the difference."

"We are pleased that accounting officers and authorities have resolved three of the 45 reported material irregularities and are dealing appropriately with 33 of them. This signals a behavioural change towards responding in a decisive and timely manner to our findings "said Maluleke.

The is a process we follow throughout the year and we don't wait for the next audit circle to understand how far is the process of addressing these material irregularities.

In addition, we have also included recommendations in the audit reports of four auditees on actions that should be taken. This is intended to resolve eight material irregularities where we concluded that appropriate action was not being taken. We also express concerns about the delays at some auditees in resolving material irregularities as a result of instability at the level of accounting officer or authority.

"There should be urgency in dealing with material irregularities to prevent further wastage, recover money and effect consequences for wrongdoing and all role players should thus work together to ensure the swift resolution of these matters' further said Maluleke.

Maluleke emphasised that "we are fully committed to the implementation of the enhanced powers given to our office, without fear, favour or prejudice as we have done over the years. The success of our amended powers will become evident when a culture of responsiveness, consequence management, good governance and accountability by accounting officers and authorities become the norm rather than the ideal."

D. Provincial audit outcomes

The AG's report notes that "overall, there is still a need to embed preventative controls (in all provinces) as this remains an essential element of accountability".

Below is a glimpse, in alphabetical order, of how the various provinces performed:

Eastern Cape

There were four improved audit outcomes in the province and one auditee that regressed. The AG notes that the improvements were due to leadership implementing commitments and oversight in the province being "more involved and accountable, but preventative controls still need attention".

The poor internal control environment negatively affected the outcomes at the key service delivery departments, namely Health, Transport and Education, and transgressions of legislation at these departments also had an adverse impact on how they spent the money allocated to them.

Free State

Three auditees improved their outcomes while one regressed for the first time since 2016-17, the province produced a clean audit. This is the second consecutive year of improvement in the province, but the AG cautioned that a "lack of accountability continued to result in pervasive non-compliance (especially relating to procurement and deteriorating financial health".

The culture of no consequences has been created through the political and administrative leadership's inability to implement consequence management for the pervasive non-compliance with legislation. Thus, the environment was vulnerable to misappropriation, wastage and the abuse of state funds. The AG called on the political leadership to "lead from the front and ensure that the administrative leadership is held accountable for their actions – "proper planning and budgeting, effective staff performance management as well as firm and timely consequences for poor performance and transgressions should be implemented".

Gauteng

There was no movement from the previous financial year as the four auditees that improved were offset by the four that regressed. The AG says "Inadequate monitoring of preventative controls and insufficient consequence management resulted in a stagnation".

The AG said it was encouraging that there was a continued improvement in the quality of the financial statements submitted for auditing, which can be attributed to regular reporting, adequate review, proper record management, and the use of governance structures to assist with reviews. In order to sustainably improve audit outcomes, we again encourage leadership to focus on the monitoring of preventative controls and ensure that transgressions are addressed through timely investigations and consequence management, especially in the area of procurement management.

KwaZulu-Natal

Five auditees improved their audit outcomes while one regressed. Maluleke says "there are progressive trends visible in the province but greater discipline is required in implementing basic preventative controls that will translate into sustainable improvements."

Alack of consequences management continued to trigger the high levels of non-compliance and irregular expenditure.

Limpopo

There was a notable improvement in audit outcomes as auditees continued to enhance their control environment and the provincial treasury strengthened oversight –as a result the audit outcomes of six auditees improved. Compliance with laws and regulations remained a challenge, as administrative leadership and senior management were slow in implementing corrective actions to address such findings, resulting in repeat audit findings.

Maluleke says the provincial leadership must "continue to strengthen preventative, detective and corrective controls at those auditees that have not achieved clean audits; and must intensify corrective actions and consequence management where deficiencies and non-compliance are noted to sustain and improve on these outcomes".

Mpumalanga

The province audit outcomes reflected a slight improvement of three auditees and one regressed but preventative controls are still not embedded at most auditees, resulting in erratic audit outcomes – leadership involvement is required to drive accountability and improve audit outcomes.

Maluleke says her office continued to raise concerns about weaknesses in controls around planning for infrastructure development and inadequate monitoring and/or project management controls.

Northern Cape

Two auditees improved their audit outcomes while one regressed, which is a step in the right direction, but the journey remains long. The AG has called on the provincial and administration leadership to "ensure accounting officers strengthen preventative controls, with a focus on the prevention and detection of irregular expenditure".

The continued reliance on the audit process was still evident as more than half of the departments could not submit quality financial statements – it also clearly indicates that the required key daily disciplines, record management and controls were not in place.

North West

Two auditees improved their outcomes while one regressed. This is an encouraging trend, but there is a need to embed preventative controls and promote a culture of consequence management. Overall, departments with financially unqualified opinions increased for the first time in two years, with the provincial treasury managing to maintain its clean audit status.

The AG says "there is also a need for accountability in order for the province to do away with the disclaimer of opinion currently obtained by five auditees," she cautions.

Western Cape

The Western Cape continued to produce the best results with 70% clean audits. Every auditee in the province submitted their annual financial statements on time for auditing and, except for one without requiring any material corrections thereto. This is a reflection of the institutionalised controls over the financial statements preparation processes.

The AG says "there has been a solid and consistent pattern of good audit outcomes in the Western Cape but the rise in irregular expenditure is of concern. The increase was due to non-compliance with supply chain management prescripts."

E. Conclusion

Maluleke says she is encouraged by the government and oversight structures attention on the weaknesses identified by her office, however said these have not shown any sustained improvement. She therefore, remain concerned that there is little improvement even after she pointed to the challenges in the previous financial year.

A continued call to act on accountability, which we believe will lead us to improvement and greater efficiency with public scares resources.

"As the national audit office, our role is to assist the accounting officers and authorities in achieving positive audit outcomes, which will strengthen accountability and improve service delivery to the citizens we serve. That has been our objective for many years and we will remain steadfast in that mission. However, where there are failures and unwillingness to act, we will have to employ the instruments we have been given in our enhanced mandate to enforce accountability.

"We will pay extra attention throughout the year to identify material irregularities and ensure that the accounting officers and authorities implement and see through their commitments on the report. We will, where we feel there is no progress, invoke the instruments in the law, to ensure that there is appropriate and timely accountability".

"We remain committed to working tirelessly within our new mandate to strengthen financial and performance management in national and provincial government, emphasising the need for accountability and doing the basics right in a manner that will eventually benefit the deserving citizens of our country," concludes Maluleke.

End.

Issued by: Auditor-General of South Africa

Contact: Africa Boso 0713653024 Africab@agsa.co.za

Follow the AGSA on Twitter: @AuditorGen_SA

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

About the AGSA: The AGSA is the country's supreme audit institution. It is the only institution that, by law, has to audit and report on how government is spending taxpayers' money. This has been the focus of the AGSA since its inception in 1911 – the organisation celebrated its 100-year public sector auditing legacy in 2011.