

# **REPORT OF THE AUDITOR-GENERAL TO PARLIAMENT ON THE PROPERTY MANAGEMENT TRADING ENTITY**

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I was engaged to audit the financial statements of the Property Management Trading Entity set out on pages ... to ..., which comprise the statement of financial position as at 31 March 2013, the statement of financial performance, statement of changes in net assets, the cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Public Finance Management Act of South Africa, 1999 (Act No. 1 of 1999) (PFMA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor-General's responsibility**

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

### **Basis for disclaimer of opinion**

#### **Irregular expenditure**

4. Section 38(1)(a)(iii) of the PFMA requires the entity to implement and maintain an appropriate procurement and provisioning system that is fair, equitable, transparent, competitive and cost-effective. Furthermore, section 40(3)(b)(i) of the PFMA requires the entity to include particulars of all irregular expenditure that had occurred during the financial year in its financial statements.
5. I was unable to obtain sufficient appropriate audit evidence for irregular expenditure as the entity did not have an adequate system for identifying and recognising all irregular expenditure. I was unable to confirm the irregular expenditure amount by alternative means. Consequently, I was unable to determine whether any adjustment relating to irregular expenditure stated at R2 609 711 000 (2012: R1 410 817 000) in note 22 to the financial statements was necessary.

#### **Fruitless and wasteful expenditure**

6. Section 40(3)(b)(i) of the PFMA requires the entity to include particulars of all fruitless and wasteful expenditure that had occurred during the financial year in its financial statements.
7. I was unable to obtain sufficient appropriate audit evidence for fruitless and wasteful expenditure as the entity did not have an adequate system for identifying and recognising all fruitless and wasteful expenditure. I was unable to confirm the fruitless and wasteful expenditure amount by alternative means. Consequently, I was unable to determine whether any adjustment relating to fruitless and wasteful expenditure stated at R254 514 000 (2012: R239 311 000) in note 21 to the financial statements was necessary.



### **Receivables and revenue from exchange transactions**

8. I was unable to obtain sufficient appropriate audit evidence that management had properly charged and accounted for receivables and revenue for accommodation charges: leasehold due to the status of the accounting records. Some of the lease agreements were not available for audit purposes. Furthermore, the amounts disclosed are based on data from the Property Management Information System (PMIS), which did not agree with information per actual signed lease agreements.
9. In addition, I was unable to obtain sufficient appropriate audit evidence regarding construction revenue because the entity was unable to provide sufficient appropriate audit evidence in support of the amount recorded.
10. I was unable to confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment to the following items in the financial statements was necessary:
  - Accommodation charges: leasehold receivable stated at R473 509 000 (2012: R450 400 000) in note 3.
  - Prepaid expenses stated at R339 082 000 (2012: R88 490 000) in note 3.
  - Construction contracts receivables stated at R292 497 000 (2012: R396 378 000) in note 5.
  - Accommodation charges: leasehold revenue stated at R3 113 217 000 (2012: R2 968 905 000) in note 14.
  - Construction revenue stated at R2 351 326 000 (2012: R3 017 957 000) in note 14.

### **Operating lease assets and associated liabilities**

11. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for operating lease assets and associated liabilities as well as operating lease commitments due to the status of the accounting records. Some of the lease agreements were not available for audit purposes. Furthermore, the amounts disclosed are based on data from the Property Management Information System (PMIS), which did not agree with information per actual signed lease agreements.
12. I was unable to confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment to the following items in the financial statements was necessary:
  - Operating lease assets and liabilities stated at R892 499 000 (2012: R859 393 000) in note 6.
  - Operating lease commitments stated at R7 154 054 000 (2012: R8 642 128 000) in note 6.
  - Accruals stated at R 1 112 729 000 (2012: R905 187 561 000) in note 9.
  - Operating leases expenditure stated at R3 341 967 000 (2012: R3 315 087 000) in note 16.

### **Retention liability**

13. The entity did not correctly recognise all outstanding amounts meeting the definition of a liability in accordance with Generally Recognised Accounting Practice, GRAP 1, *Presentation of financial statements*. Consequently, retention liability is misstated by an



estimated amount of R156 142 482 (2012: R282 778 068). There is also a consequential impact on construction expenditure and the accumulated surplus.

#### **Disclaimer of opinion**

14. Because of the significance of the matter described in the Basis for disclaimer of opinion paragraph, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

#### **Emphasis of matter**

15. I draw attention to the matters below. My opinion is not modified in respect of these matters.

#### **Going concern**

16. Note 1.6 to the financial statements indicates that as of 31 March 2013, the PMTE is in a net liability position. This condition, along with other matters as set forth in note 1.6, indicates the existence of a material uncertainty that may cast significant doubt on the trading entity's ability to operate as a going concern.

#### **Restatement of corresponding figures**

17. As disclosed in note 29 to the financial statements, the corresponding figures for 31 March 2012 have been restated as a result of errors discovered during 2013 in the financial statements of the Property Management Trading Entity at, and for the year ended, 31 March 2012.

#### **Material impairments**

18. As disclosed in note 3 to the financial statements, material impairments to the amount of R82 971 000 were provided for as a result of irrecoverable receivables.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

19. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

#### **Compliance with laws and regulations**

20. I performed procedures to obtain evidence that the entity had complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations, as set out in the general notice issued in terms of the PAA, are as follows:

#### **Strategic planning and performance management**

21. The accounting officer of the Department of Public Works did not finalise and approve the business case for running the trading entity and consequently did not formulate a policy and reporting framework for the head of the trading entity in accordance with the requirements of Treasury Regulation 19.3.1.

#### **Annual financial statements, performance and annual reports**

22. The financial statements submitted for auditing were not prepared in accordance with



the prescribed financial reporting framework and supported by full and proper records, as required by section 40(1)(a) and (b) of the PFMA.

Material misstatements of accruals and expenditure identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records provided, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a disclaimer of audit opinion.

### **Procurement and contract management**

23. Goods and services with a transaction value of below R500 000 were in certain instances procured without obtaining the required number of price quotations, as required by Treasury Regulation 16A6.1.
24. Goods and services of a transaction value of above R500 000 were in certain instances procured without inviting competitive bids, as required by Treasury Regulations 16A6.1. A number of deviations were approved even though it was not impractical to invite competitive bids, in contravention of Treasury Regulation 16A6.4.
25. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act and CIDB regulation 18.
26. Persons in service of the trading entity who had a private or business interest in contracts awarded by the trading entity failed to disclose such interest, as required by Treasury Regulation 16A8.4 and Public Service Regulation 3C.
27. Persons in service of the trading entity who had a private or business interest in contracts awarded by the trading entity participated in the process relating to that contract, in contravention of Treasury Regulation 16A8.4.
28. Allegations of fraud, corruption, improper conduct and failure to comply with the supply chain management system made against officials and role players in the supply chain management system were not in all instances investigated as required by Treasury Regulation 16A9.1(b).
29. Appropriate action was not in all instances taken against officials and role players in the supply chain management system where investigations proved fraud and corruption, improper conduct and failure to comply with the supply chain management system, as required by Treasury Regulation 16A9.1(b)(i).
30. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements as the entity did not implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information was accessible and available to evaluate compliance.

### **Expenditure management**

31. The accounting officer did not take effective steps to prevent irregular and fruitless and wasteful expenditure, as required by section 38(1)(c)(ii) of the PFMA and Treasury Regulation 9.1.1.
32. Effective and appropriate disciplinary steps were not taken against officials who made or permitted irregular expenditure, as required by section 38(1)(h)(iii) of the PFMA and



### **Revenue management**

33. The accounting officer did not develop and implement appropriate processes that provide for the identification, collection, recording, reconciliation and safeguarding of information about revenue to ensure that all money due to the trading entity was collected as per the requirements of section 38(1)(c)(ii) of the PFMA and Treasury Regulation 7.2.1.
34. The accounting officer did not take effective and appropriate steps to collect all money due, as required by section 38(1)(c)(i) of the PFMA and Treasury Regulations 11.2.1, 15.10.1.2(a) and 15.10.1.2(e).

### **Financial misconduct**

35. Investigations were not conducted into all allegations of financial misconduct committed by officials, as required by Treasury Regulation 4.1.1.
36. Investigations into allegations of financial misconduct against officials were not instituted within 30 days of discovery thereof, as required by Treasury Regulation 4.1.2.
37. Disciplinary hearings were not held for financial misconduct committed by officials, as required by Treasury Regulation 4.1.1.

### **Banking and cash management**

38. The entity's main bank account was overdrawn throughout the reporting period, in contravention of Treasury Regulation 19.2.3.

### **Internal control**

39. I considered internal control relevant to my audit of the financial statements and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion and the findings on compliance with laws and regulations included in this report.

### **Leadership**

40. Certain critical appointments were only made in the last quarter of the financial year, thus instability in key leadership positions for the first part of the financial year had a negative impact in providing effective leadership in the department.
41. Leadership did not exercise effective oversight of financial and performance reporting and compliance and related internal controls.
42. Leadership did not apply effective consequence management for transgressions with regard to non-performance and non-compliance throughout the financial year.
43. Leadership did not in all instances establish and communicate policies and procedures to enable and support the understanding and execution of internal objectives, processes and responsibilities.

### **Financial and performance management**

44. Proper record keeping was not always implemented in a timely manner to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting.

45. Implemented controls over daily and monthly processing and reconciling of transactions were not effective in all instances.
46. Regular, accurate and complete financial and performance reports supported and evidenced by reliable information were not prepared throughout the year.
47. The review and monitoring of compliance with applicable laws and regulations were ineffective.

#### **Governance**

48. Risk management activities, including the consideration of IT risks and fraud prevention, were not effectively conducted. A risk strategy to address identified risks was not developed and monitored throughout the financial year.
49. The internal audit unit was not adequately resourced to ensure that it could effectively assist in identifying internal control deficiencies and developing recommendations in respect of corrective action to be taken to address the internal control deficiencies identified. This has also resulted in the continued backlog in internal investigations.

#### **OTHER REPORTS**

##### **Investigations**

50. Numerous internal allegations, mainly relating to transgressions with respect to supply chain management, potential fraud and financial misconduct, are investigated on an ongoing basis.
51. An ongoing investigation is being conducted to probe the alleged abuse of urgent and emergency procurement as well the utilisation of sole suppliers. The investigation aims to establish whether there was collusion between officials and service providers and to determine any reckless spending of funds. The investigation is being conducted in phases, with nine reports having been finalised to date, while the majority were still ongoing at the reporting date. The department is in the process of instituting disciplinary action in respect of the finalised reports.

*Auditor-General*

Pretoria

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