**DRAFT MANAGEMENT REPORT**

**Property Management Trading Entity**

**31 MARCH 2016**

**Communicated to management on: 15 July 2016**

**MANAGEMENT REPORT**

**Property Management Trading Entity**

**31 March 2016**

**Discussed with management on:**

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**MANAGEMENT REPORT TO THE ACCOUNTING OFFICER ON THE AUDIT OF THE PROPERTY MANAGEMENT TRADING ENTITY FOR THE YEAR ENDED 31 MARCH 2016**

**INTRODUCTION**

1. Our responsibility is to:

* express an opinion on the separate financial statements
* express a conclusion in the management report on the usefulness and reliability of the reported performance information for selected programmes, and report the material findings in the auditor’s report
* report on material findings relating to compliance with specific requirements in key applicable legislation, as set out in the general notice issued in terms of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA).

Our engagement letter sets out our responsibilities and those of the accounting officer in detail.

1. This management report includes audit findings arising from the audit of the financial statements, reporting on predetermined objectives and compliance with legislation for the year ended 31 March 2016. These findings were communicated to management and the report details management’s response to these findings. The report includes information on the internal control deficiencies that we identified as the root causes of the matters reported. Addressing these deficiencies will help to improve the audit outcome.
2. This management report consists of an executive summary and annexures containing the detailed audit findings.
3. The purpose of the management report is to communicate audit findings to the accounting officer and does not constitute public information. The auditor’s report is finalised only after the management report has been communicated. All matters included in this report that relate to the auditor’s report remains in draft form until the final auditor’s report is signed. In adherence to section 50 of the PAA, we do not disclose any information obtained during the audit and contained in this management report.

**EXECUTIVE SUMMARY**

**SECTION 1: Interactions with stakeholders responsible for oversight and governance**

1. During the audit cycle, we met with the following key stakeholders responsible for oversight and governance to communicate matters relating to the audit outcome of the Trading Entity:

|  |  |
| --- | --- |
| **Stakeholder** | **Number of interactions** |
| Speaker of the portfolio committee on Public Works | 2 |
| Standing committee on public accounts | 0 |
| Minister of Public Works | 3 |
| Director-general | 3 |
| Audit committee | 10 |

1. At these interactions we discussed the terms of the audit engagement (with specific emphasis on the roles and responsibilities of the auditor and management as well as those charged with governance), overall audit strategy including the proposed nature, timing and extent of audit procedures to be performed, risk assessment (including fraud risk assessment) and the effectiveness of internal control. Discussions were held relating to the challenges around immovable assets, predetermined objectives and the full implementation of the accrual accounting system. Audit progress and findings were discussed on a continuous basis and the audit outcome for 2015-16 will be discussed prior to the finalisation of the audit report.
2. Some of the stakeholders made commitments to implement initiatives that can improve the audit outcome. The commitments given and the progress of previous commitments are included in part F of section 2, which deals with the assessment of assurance providers.

**SECTION 2: Matters relating to the auditor’s report**

## 2.1 MISSTATEMENTS IN THE FINANCIAL STATEMENTS

1. We identified material misstatements in the financial statements during the audit. These misstatements were not prevented or detected by the Trading Entity’s system of internal control. These material misstatements also constitute non-compliance with section 40(1) of the Public Finance Management Act (PFMA).
2. The misstatements that were not corrected form the basis for the qualified/adverse/disclaimer of opinion on the financial statements.

| **Material misstatement** | | | **Impact**  **R**  current year | **Impact**  **R**  prior year |
| --- | --- | --- | --- | --- |
| **Financial statement item** | **Finding**  (Include a brief description of the misstatement as per the findings and the auditor’s report. Include the reasons for the auditee not correcting the misstatement when applicable.) | **Occurred in prior year**  (Insert Yes/No) |
| **Material misstatements not corrected** | | | | |
| **Non-current assets** |  |  |  |  |
| Property, plant and equipment | Property reports from Light-stone | No | 42 250 912 186 |  |
|  | Inappropriate audit evidence (Actual errors) | No | 66 011 040 |  |
|  | Exceptions identified through comparison of deeds registry and immovable Assets register | No | Not quantifiable |  |
|  | Incorrect building counts as per IAR | No | 382 808 988 |  |
|  | Differences between the financial statements and the supporting schedules | Yes | 101 593 379 | 101 897 228 |
|  | Differences between valuation recalculation and fixed asset register | No | 689 013 566 |  |
|  | Assets not shown in the disposals and/or opening balance of the Property Plant and Equipment | No | Not quantifiable |  |
|  | Reconciliation between PMIS and SAGE payments of property rates and taxes and the immovable assets register | Yes | 894 843 997 | 835 257 000 |
|  | Application of Deemed cost and transitional provisions of Directive two to the Immovable assets | Yes | 112 419 625 000 | 111 002 776 000 |
|  | Addition of a complete asset recognised as asset under construction | No | 694 835 270 |  |
|  | Reconciliation between WCS and SAGE payments for accrual assets | No | 3 007 933 020 |  |
|  | WCS projects capitalised during the transitional provisions of Directive two on buildings and improvements | No | 189 909 295 |  |
|  | Differences between the building indices calculation of average vacant land ratios and auditor’s calculations | No | 1 194 389 264 |  |
|  | Information requested could not be provided (COFF 107) | Yes | 432 878 000 | 406 334 000 |
|  |  |  |  |  |
| Investment Properties | Information requested could not be provided (COFF 91) | No | 5 201 149 149 |  |
|  |  |  |  |  |
| **Current assets** |  |  |  |  |
| Revenue accrual | There is insufficient documentary evidence that recovery of under claims from client departments is probable, as this is contingent on the underpayment to landlord being finalised. | No | 326 859 638 |  |
| Prepayments | Schedule supporting the financial statements does not agree with the confirmation letters signed by the municipality | No | 192 229 376.86 |  |
| **Current liabilities** |  |  |  |  |
| Deferred revenue | Revenue not recognised on projects completed before year end | No | 125 974 364 |  |
|  |  |  |  |  |
| Accruals | Payment advices for Accrual assets not submitted for audit purposes | No | 55 121 385 |  |
|  | Proof of services rendered for WCS Accruals not submitted for audit purposes | No | 3 942 774 |  |
| Provision | Schedule supporting the financial statements does not agree with the confirmation letters signed by the municipality | No | 113 864 594.57 |  |
|  |  |  |  |  |
|  |  |  |  |  |
|  |  |  |  |  |
| Expenditure -Property maintenance and consultants | Transactions that were incurred in the current year under review were not recorded in the accrual expenditure | Yes | Understatement of 10 119 346 |  |
|  |  |  |  |  |
| **Disclosure** |  |  |  |  |
| Capital commitments | Commitments for contracts awarded before year end not included on commitment listing | No | Understatement of 153 096 722 |  |
|  |  |  |  |  |
| Fruitless and wasteful expenditure | Overpayments on leased buildings were made to the extent that the total amount paid in respect of the lease was greater than the total payments required in terms of the lease agreement | Yes | 75 451 668 |  |
| Contingent liabilities | Disclosures in the incorrect financial years - municipal services and property rates | No | 104 518 000 | 104 518 000 |
|  | Schedules not agreeing to the amounts disclosed - municipal services and property rates | No | 114 198 000 |  |
| Irregular expenditure | Payment made toward suppliers with expired lease contracts, additional we could not trace the payments to the irregular expenditure register | Yes | 79 097 338 |  |
| Transaction that was identified as irregular expenditure in the prior year however it not included in the current year irregular register | No | 1 945 456 |  |
|  |  |  |  |  |

**2.2 MATTERS TO BE BROUGHT TO THE ATTENTION OF USERS**

Emphasis of matter paragraphs

1. The following emphasis of matter paragraphs will be included in our auditor’s report to draw the users’ attention to matters presented or disclosed in the financial statements:

**Material impairments**

1. As disclosed in note 21 to the financial statements, material losses to the amount of   
   R355 766 000 were incurred as a result of a write-off of irrecoverable trade debtors.

**Irregular expenditure**

1. As disclosed in note 31 to the financial statements, irregular expenditure amounting to R27 256 513 which is not recoverable was written off (not condoned), as it was impracticable to go through the prescribed process in terms of the Guideline on Irregular Expenditure issued by the National Treasury.

**Restatement of corresponding figures**

1. As disclosed in note 36 to the financial statements, the corresponding figures for   
   31 March 2015 were restated as a result of errors discovered during 2016 in the financial statements of the Property Management Trading Entity (PMTE) at, and for the year ended, 31 March 2016.

**Transfer of functions**

1. The Department of Public Works (DPW) transferred certain property management functions, including the related assets, liabilities and staff, to the PMTE as at 1 April 2013. An additional transfer took place as at 1 April 2014. The effect of these transfers is detailed in note 37 of the financial statements.

Additional matter paragraphs

1. The following additional matter paragraphs will be included in our auditor’s report to draw the users’ attention to matters regarding the audit, the auditor’s responsibilities and the auditor’s report:

**2.3 REPORT ON PREDETERMINED OBJECTIVES**

Introduction

1. As required by sections 4 and 20 of the PAA, read with the general notice issued in terms thereof, we have audited the reported performance information of the following selected programmes presented in the annual performance report of the entity for the year ended 31 March 2016:
2. Programme 3: Construction Project Management on pages x
3. Programme 4: Real Estate Management on pages x
4. Programme 6: Facilities Management on pages x
5. We conducted our audit in accordance with the International Standards on Assurance Engagements (ISAE) 3000: Assurance engagements other than audits or reviews of historical financial information.
6. We evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury’s annual reporting principles and whether the reported performance was consistent with the planned programmes. We further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury’s *Framework for managing programme performance information* (FMPPI).
7. We assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
8. We believe that the evidence obtained from the work performed provides an appropriate basis for the reasonable assurance conclusions on the usefulness and reliability of the reported performance information expressed below.

Summary of audit conclusions

1. The following is a summary of our conclusions on the usefulness and reliability of the reported performance information:

| **Selected programme** | **Usefulness** | **Reliability** |
| --- | --- | --- |
| Programme 3: Construction Project Management | Adverse | Disclaimer |
| Programme 4: Real Estate Management | Adverse | Disclaimer |
| Programme 6: Facilities Management | Adverse | Disclaimer |

**Programme 3: Construction Project Management**

**Basis for adverse conclusion on usefulness**

Presentation of performance information

1. The reasons provided for variances between planned targets and actual achievements were not reliable when compared to the source information.

Consistency of objectives

1. Treasury Regulation 30.1.3(g) requires the annual performance plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% reported objectives were not consistent with those in the approved annual performance plan.

Measurability of indicators

1. The FMPPI requires that performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use. A total of 100% indicators were not well defined.
2. And the processes and systems that produced the indicator should be verifiable, as required by the FMPPI. A total of 100 % indicators were not verifiable*.*

**Adverse conclusion on usefulness**

1. In our opinion, because of the significance of the matters described in the basis for adverse conclusion paragraphs, the reported performance information of programme 3: construction project management presented in the annual performance report is not useful in accordance with the identified performance management and reporting framework.

**Basis for disclaimer of conclusion on reliability**

Reliability of reported performance information

1. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure reliable reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information

**Disclaimer of conclusion on reliability**

1. Because of the significance of the matter described in the basis for disclaimer of conclusion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for conclusion. Accordingly, we do not express a conclusion on the reliability of Programme 3: Construction Project Management.

**Programme 4: Real Estate Management**

**Basis for adverse conclusion on usefulness**

Presentation of performance information

1. The reasons provided for variances between planned targets and actual achievements were not reliable when compared to the source information.

Consistency of objectives

1. Treasury Regulation 30.1.3(g) requires the annual performance plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% reported objectives were not consistent with those in the approved annual performance plan

Measurability of indicators

1. The FMPPI requires that performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use. A total of 100% indicators were not well defined.
2. And the processes and systems that produced the indicator should be verifiable, as required by the FMPPI. A total of 100 % indicators were not verifiable*.*

**Adverse conclusion on usefulness**

1. In our opinion, because of the significance of the matters described in the basis for adverse conclusion paragraphs, the reported performance information of programme 4: real estate management presented in the annual performance report is not useful in accordance with the identified performance management and reporting framework.

**Basis for disclaimer of conclusion on reliability**

Reliability of reported performance information

1. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure reliable reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information

**Disclaimer of conclusion on reliability**

1. Because of the significance of the matter described in the basis for disclaimer of conclusion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for conclusion. Accordingly, we do not express a conclusion on the reliability of Programme 4: Real Estate Management

**Programme 6: Facilities Management**

**Basis for adverse conclusion on usefulness**

Presentation of performance information

1. The reasons provided for variances between planned targets and actual achievements were not reliable when compared to the source information.

Consistency of objectives

1. Treasury Regulation 30.1.3(g) requires the annual performance plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% reported objectives were not consistent with those in the approved annual performance plan

Measurability of indicators

1. The FMPPI requires that performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use. A total of 100% indicators were not well defined.
2. And the processes and systems that produced the indicator should be verifiable, as required by the FMPPI. A total of 100 % indicators were not verifiable*.*

**Adverse conclusion on usefulness**

1. In our opinion, because of the significance of the matters described in the basis for adverse conclusion paragraphs, the reported performance information of programme 6:facilities Management presented in the annual performance report is not useful in accordance with the identified performance management and reporting framework.

**Basis for disclaimer of conclusion on reliability**

Reliability of reported performance information

1. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure reliable reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves as to the reliability of the reported performance information. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information

**Disclaimer of conclusion on reliability**

1. Because of the significance of the matter described in the basis for disclaimer of conclusion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for conclusion. Accordingly, we do not express a conclusion on the reliability of programme 6: facilities management

Additional matters

1. We draw attention to the following matter. Our conclusion is not modified in respect of these matters

Achievement of planned targets

1. Refer to the annual performance report on pages x to x; x to x for information on the achievement of planned targets for the year. This information should be considered in the context of the adverse and disclaimer of conclusions expressed on the usefulness and reliability of the reported performance information in paragraphs x; x; x of this report.

Adjustment of material misstatements

1. We identified material misstatements in the annual performance report submitted for auditing. As management subsequently corrected only some of the misstatements, we raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are included in the basis for disclaimer of conclusions paragraphs.

Unaudited supplementary information

1. The supplementary information set out on pages x to x does not form part of the annual performance report and is presented as additional information. We have not audited these schedules and, accordingly, we do not express a conclusion on them.

Audit findings in the auditor’s report

1. We will report all the audit findings included under the basis for conclusion and additional matter sections of this report in the auditor’s report.

**2.4 FINDINGS ON COMPLIANCE WITH LEGISLATION**

1. Included below are material findings on compliance with selected specific requirements of applicable legislation, as set out in the general notice issued in terms of the PAA.

Annual financial statements

1. The financial statements submitted for auditing were not prepared in accordance with the prescribed financial reporting framework and/or supported by full and proper records as required by section 40(1) (a) and (b) of the Public Finance Management Act.
2. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected, which resulted in the financial statements receiving a qualified/adverse/disclaimer audit opinion.

Procurement and contract management

1. Sufficient appropriate audit evidence could not be obtained that all contracts and/ or 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
2. Goods and services with a transaction value below R500 000 were procured without obtaining the required price quotations, as required by Treasury Regulation 16A6.1.
3. Goods and services of a transaction value above R500 000 were procured without inviting competitive bids, as required by Treasury Regulations 16A6.1. A number of deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of Treasury regulation 16A6.4.
4. Invitations for competitive bidding were not always advertised for a required minimum period, as required by Treasury Regulations 16A6.3(c).
5. Contracts were awarded to bidders who did not submit a declaration of past supply chain practices such as fraud, abuse of SCM system and non-performance, which is prescribed in order to comply with Treasury regulation 16A9.2
6. Contracts and quotations were awarded to suppliers whose tax matters had not been declared by the South African Revenue Services to be in order as required by Treasury Regulations 16A9.1(d) and the Preferential Procurement Regulations.
7. Contracts were awarded to bidders based on points given for criteria that were not stipulated and/or differed from those stipulated in the original invitation for bidding, in contravention of Treasury Regulations 16A6.3(a) and the Preferential Procurement Regulations.
8. Contracts were awarded to bidders based on preference points that were not allocated and/or calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
9. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, which is prescribed in order to comply with Treasury regulation 16A8.3.
10. Construction contracts were awarded in certain instances to contractors that did not qualify for the contract in accordance with section 18(1) of the CIDB Act and CIDB regulations 17 and 25(7A)
11. Persons in service of the trading entity whose close family members, partners or associates 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 .
12. Measures for combating the abuse of the supply chain management (SCM) system were not implemented as required by Treasury Regulations 16A9.1 in that awards were made to providers who committed a corrupt or fraudulent act in competing for the contract.

Expenditure Management

1. Effective steps were not taken to prevent irregular expenditure, as required by section 38(1)(c)(ii) of the Public Finance Management Act and Treasury Regulation 9.1.1

Revenue Management

1. Effective and appropriate steps were not taken to collect all money due, as required by section 38(1)(c)(i) of the Public Finance Management Act and Treasury Regulations 11.2.1, 15.10.1.2(a) and 15.10.1.2(e).
2. Sufficient appropriate audit evidence could not be obtained that immovable state property was let at market-related tariffs, as required by Treasury Regulation 16A7.4.

**2.5 INTERNAL CONTROL**

1. Below is our assessment of implementing the drivers of internal control based on significant deficiencies identified during our audit of the financial statements, the annual performance report and compliance with legislation. Significant deficiencies occur when internal controls do not exist, are not appropriately designed to address the risk, or are not implemented. These either had caused, or could cause, the financial statements or the annual performance report to be materially misstated, and material instances of non-compliance with legislation to occur.
2. The internal controls were assessed as follows:

|  |  |
| --- | --- |
|  | The required preventative or detective controls were in place. |
|  | Progress was made on implementing preventative or detective controls, but improvement is still required, or actions taken were not or have not been sustainable. |
|  | Internal controls were either not in place, were not properly designed, were not implemented or were not operating effectively. Intervention is required to design and/or implement appropriate controls. |

1. The movement in the status of the drivers from the previous year-end to the current year-end is indicated collectively for each of the three audit dimensions under the three fundamentals of internal control. The movement is assessed as follows:

|  |  |
| --- | --- |
|  | Improved |
|  | Unchanged |
|  | Regressed |

|  | **Financial statements** | | **Performance reporting** | | **Compliance with legislation** | |
| --- | --- | --- | --- | --- | --- | --- |
|  | **Current year** | **Prior year** | **Current year** | **Prior year** | **Current year** | **Prior year** |
| **Leadership** | | | | | | |
| **Overall movement from previous assessment** |  | |  | |  | |
| * Provide effective leadership based on a culture of honesty, ethical business practices and good governance, and protecting and enhancing the best interests of the entity |  |  |  |  |  |  |
| * Exercise oversight responsibility regarding financial and performance reporting and compliance as well as related internal controls |  |  |  |  |  |  |
| * Implement effective human resource management to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored |  |  |  |  |  |  |
| * Establish and communicate policies and procedures to enable and support the understanding and execution of internal control objectives, processes and responsibilities |  |  |  |  |  |  |
| * Develop and monitor the implementation of action plans to address internal control deficiencies |  |  |  |  |  |  |
| * Establish an information technology governance framework that supports and enables the business, delivers value and improves performance |  |  |  |  |  |  |
| **Financial and performance management** | | | | | | |
| **Overall movement from previous assessment** |  | |  | |  | |
| * Implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting |  |  |  |  |  |  |
| * Implement controls over daily and monthly processing and reconciling transactions |  |  |  |  |  |  |
| * Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information |  |  |  |  |  |  |
| * Review and monitor compliance with applicable legislation |  |  |  |  |  |  |
| * Design and implement formal controls over information technology systems to ensure the reliability of the systems and the availability, accuracy and protection of information |  |  |  |  |  |  |
| **Governance** | | | | | | |
| **Overall movement from previous assessment** |  | |  | |  | |
| * Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of information technology risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored |  |  |  |  |  |  |
| * Ensure that there is an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and recommends corrective action effectively |  |  |  |  |  |  |
| * Ensure that the audit committee promotes accountability and service delivery through evaluating and monitoring responses to risks and overseeing the effectiveness of the internal control environment, including financial and performance reporting and compliance with legislation |  |  |  |  |  |  |

1. The table below provides the overall status of the drivers of key controls and is followed by details of the significant deficiencies identified.

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  |  | | Status of the drivers of internal controls | | | | | | | | | |  |  |
| **Leadership** | | | |  |  |  | **Financial and performance management** |  |  |  | **Governance** |  |  |
| Effective leadership culture | | | | |  |  | Proper record keeping | |  |  | Risk management | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| Oversight responsibility | | | | |  |  | Processing and reconciling controls | |  |  | Internal audit | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| HR management | | | | |  |  | Regular reporting | |  |  | Audit committee | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| Policies and procedures | | | | |  |  | Compliance monitoring | |  |  |  | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| Audit action plans | | | | |  |  | IT system controls | |  |  |  | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| IT governance | | | | |  |  |  | |  |  |  | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| Improved | | | | |  |  | Unchanged | |  |  | Regressed | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| Improved | | | | |  |  | Unchanged | |  |  | Regressed | |  |
|  | | | | |  |  |  | |  |  |  | |  |
| Good | | | | |  |  | Concerning | |  |  | Intervention required | |  |
|  |  | |  |  | | | | | | | | | | | |

Leadership

**Effective leadership culture**

1. Although a new head of the trading entity was appointed during May 2015, some senior management positions are still vacant or filled by acting incumbents. Some of the critical positions that are currently vacant are:
   * DDG: Asset Investment Management
   * DDG: Special Projects (filled by acting incumbent)
   * CD: Professional services
   * CD: Inner City Regeneration & Project Management

In addition, there are 14 senior management (SMS) positions that are currently vacant.

1. The department acknowledged that there were internal constraints within the governance, risk and compliance unit, which impacted their ability to conduct their own internal investigations. We have noted that the majority of investigations are initiated within the required time; however investigations take extremely long to finalise.

Some investigations are thus referred to Special Investigations Unit or to SAPS where criminal activities are suspected. Where follow up actions are required from the department as a result of findings from investigations (e.g. disciplinary hearings, etc.), these are not taking place on time.

1. It is a major concern that amounts paid to landlords in terms of private leased properties are still being made using the amounts from the PMIS system which was confirmed to be incorrect in most instances, a result of which landlords continue to either be over or underpaid. In the current we also noted that in some instances payments made to landlord were more than the total required over the lease period. This situation has been previously communicated to management.

**Oversight responsibility**

1. Monthly management accounts are not being prepared for the entity. Currently financial statements are only prepared twice a year (for interim and financial statements). The preparation and review of monthly management accounts will assist a great deal in the effective discharge of oversight responsibility. The full implementation of the new financial accounting software may assist in this regard.
2. The process of initially accounting for the immovable assets acquired through the transfer of functions was not adequately completed prior to the end of the financial year under review. Significant weaknesses were identified in the model utilised by the entity to account for immovable assets in line with the requirements of GRAP.
3. Compliance matters relating to supply chain management remain the most critical area of non-compliance. While cognisance is taken of the fact that a major project was undertaken in the 2013-14 year to identify all irregular expenditure incurred, there appears to be insufficient interventions in place to prevent irregular expenditure which is evidenced by the significant amount of irregular expenditure incurred as disclosed in the annual financial statements for the year ended 31 March 2016.

**Human resource management**

1. The department complied in the approval and implementation of the HR Plan. The department is however still in the process of finalising the updated organisational structure in line with the radical restructuring that took place between the department and PMTE, which amongst others includes the approval of the new programme budget structure. A migration framework was also developed, however it is yet to be implemented.
2. The process of getting the new organisational structure approved is a very comprehensive process. Widespread consultations were held with internal and external stakeholders, amongst others the various branches in the department/PMTE and labour unions. When the process was about to be finalised a new Head of the PMTE was appointed and validly asked to also provide inputs. Initial approval has been obtained from the Minister for the department for the department to consult with DPSA. The department is currently awaiting inputs from DPSA before submitting to the Minister for final approval.

**Policies and procedures**

1. The entity should ensure that all new approved policies and procedures are adequately and timeously communicated to officials in the entity to reduce the instances of non-compliance with applicable laws and regulations. A new policy was developed to account for accruals in the prior year; however during our audit at the regions we noted that it was not consistently applied throughout all the regional offices. In addition, the policy document formulated to account for immovable assets in line with GRAP was amended during the reporting period resulting in inconsistent application.

**Action plans to address internal control deficiencies**

1. Implementation of the audit actions plan has not transpired in all instances. It is a concern that the issue of incorrect payments being made in terms of leases identified in the 2014-15 year has not yet been adequately addressed. The process of correcting the over and underpayments did not commence swiftly enough to have an impact in the current period.

**Information technology governance framework**

1. Management had formally documented policies to mitigate the risk of unauthorised access to the network and information systems. However, the information security policy had not yet been approved at the appropriate level of management.
2. The department has not formally documented and approved a disaster recovery plan. Without a comprehensive disaster recovery plan the department may be unable to recover critical business functions within an acceptable timeframe. This may result in lengthy disruptions which could affect the department’s delivery on its mandate.
3. The entity did not have appropriate controls in place to ensure that proper backups are performed and kept off-site. We found that the backup strategy process was inadequate as regional offices could not duplicate their backups.

Financial and performance management

**Proper record keeping**

1. The trading entity has not yet fully implemented the new record management system. While improvements were noted in the recovery of documents for audit purposes, it is a concern that in some instances tender/project files were kept by process owners, constraining the recoverability of the documents and increasing the risk of documentation being misplaced.
2. We also noted that the SAGE system purchased in the prior period was not yet fully implemented for the 2015-16 financial period. to record transactions in accordance with GRAP impacted the trading entity’s ability to generate information within a reasonable time and accuracy. Initiatives were in place to prepare these manual schedules or “workbooks” monthly to streamline the process and ensure that data was available when required. However, due to the volume of transactions required to be processed manually, there was still a significant risk of human error.
3. The full implementation of SAGE will also assist with the following:

* *Immovable assets* – The asset register is currently maintained on Excel which is does not have any controls over input changes etc.
* *Accruals –* These will automatically be updated on a fully implemented system, which will negate the need for the manual workbooks which are prone to human error.
* *Leases ­–* There are currently two systems being used for leases (i.e. PMIS for operational purposes and manual calculations for reporting purposes). If the relevant module of SAGE was properly utilized, this will possibly prevent the over and underpayments that are currently being made from the PMIS system.

1. The entity did not have sufficient schedules supporting actual performance in respect of their Annual Performance Report (APR). Information is still outstanding for two out of the three material programmes selected for audit.

**Daily and monthly processing and reconciling of transactions**

1. We have noted that the manual schedules submitted with the financial statements do not agree in all instances with the financial statements. In other instances, the schedules that are provided contain aggregated or summarized information and thus are not in a format that enables sampling to be performed. This is only identified by the audit team after sampling has been done, and thus requires a duplication of effort once the correct information is obtained.
2. The entity did not have an adequate system in place to collect information required to support quarterly and annual financial reports. As a result, information supporting the quarterly performance reports was only submitted for audit at year end, after findings were issued in this regard, and not at the end of every quarter as is required.

**Regular, accurate and complete financial and performance reports**

1. Currently financial statements are only prepared twice a year (for interim and financial statements).Due to the lack of full implantation of the financial accounting system, the process of preparing these financial statements is an extremely lengthy process. As a result there is a lack of credible financial reporting throughout the year to enable leadership to review and take appropriate and timeous corrective action where required. Preparing monthly management accounts will also assist management in institutionalising the controls required in order to ensure regular, accurate and complete financial reporting.
2. We were unable to perform the procedures required to obtain assurance regarding the quarterly performance reports for Quarter 1 and Quarter 2 of 2015/16, as we did not receive adequate documentation supporting the reported performance.
3. Our audit of the APR revealed that there is insufficient co-ordination Planning and Reporting sections, resulting in the documentation required to support achievements agaisnt the Annual Performance Plan (APP)

**Compliance monitoring**

1. Now that the project of identifying and reporting the historical irregular expenditure is complete, the focus of the department should be on the implementation of controls to prevent a recurrence of the situations which lead to the non-compliance with laws and regulations or deviations from prescribed supply chain management prescripts. In many instances we identified the deviations were used incorrectly.
2. Numerous instances of non-compliance have been identified in the current audit cycle, as well by internal investigations and internal audits. Leadership should enhance oversight and adopt a zero tolerance approach when it comes to non-compliance. The starting point for this would be addressing the repeated non-compliance with regards to consequence management that has been reported in the trading entity in each of the preceding three financial years.

**Information technology systems**

1. Transactions and schedules supporting the financial statements are still being prepared and processed manually, as a result all the significant transactions and balances of the entity were compiled outside of SAGE for the interim period. This is due to the fact that as of the date of this report, only the petty cash module and the payments and receipts modules have been implemented.
2. The entity is over reliant on consultants to perform key IT functions. In the event that the contractors/consultants leave the organisation, the IT department might not be able to adequately provide IT support in order to meet the department’s needs. Furthermore the high cost of maintaining contractors/ consultants may not be sustainable in the long run.
3. The payment file transfer process was currently manual and did not have encryption controls to ensure sensitive payment information was protected.

Governance

**Risk management activities and risk strategy**

1. Although a risk assessment was concluded the entity needs to do a significant amount of work to embed a culture of effective risk management. The size of the risk management department is still too small for what they need to do. Increasing the capacity of this department will enable to increase focus on regional offices where many of the risks reside.

**Internal audit**

1. The internal audit unit at the department is currently under resourced. The audits performed by this unit are thus not always completed timeously (e.g. audit on migration to new accounting system). As their audit is not complete at the time when external audit is busy with our fieldwork, we are not always able to utilize the work of internal audit.
2. We have noted from our review of the work of internal audit that management has in some instances, slow to respond to the findings of internal audit. Addressing these findings will strengthen the control environment in the department, and embed a culture of compliance within all officials.

**Audit committee**

1. The audit committee is currently effectively involved from a governance perspective in the department and entity’s turnaround process, which is an on-going project.

Summary

1. The matters above, as they relate to the basis for the [qualified/adverse/disclaimer of] opinion, findings on the annual performance report and findings on compliance with legislation, will be summarised in the auditor’s report as follows:

**Leadership**

1. Leadership did not exercise effective oversight responsibility in all instances regarding financial and performance reporting and compliance as well as related internal controls.
2. Leadership did not institute effective measures to ensure that the issue of incorrect payments being made to suppliers in respect of private leases was adequately resolved.

**Financial and performance management**

1. 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 performance reporting.
2. Regular, accurate and complete financial and performance reports that were supported by reliable information were not prepared throughout the financial year.
3. The review and monitoring of compliance with applicable laws and regulations were ineffective in certain instances.

Governance

1. Leadership must continue to focus on expanding capacity in the risk management and internal audit units to ensure optimal functioning in terms of addressing of risks and internal control deficiencies across all locations within the entity.

**2.6 ASSURANCE PROVIDERS AND STATUS OF IMPLEMENTATION OF COMMITMENTS AND RECOMMENDATIONS**

1. The annual report is used to report on the financial position of auditees, their performance against predetermined objectives and overall governance. One of the important oversight functions of Parliament is to consider auditees’ annual reports. To perform this oversight function, they need assurance that the information in the annual report is credible. To this end, the annual report includes our auditor’s report, which provides assurance on the credibility of the financial statements and the annual performance report, as well as on the auditee’s compliance with legislation.
2. Our reporting and the oversight processes reflect on past events, as it takes place after the end of the financial year. However, management, the leadership and those charged with governance contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.

We assess the level of assurance provided by these assurance providers based on the status of internal controls (as reported in section 2.5) and the impact of the different role players on these controls. We provide our assessment for this audit cycle below.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Assurance levels** | | |  |
|  | | |
| Senior management |  | ***Provides some assurance*** |
|  |  |
| Accounting officer | ***Provides some assurance*** |
|  |  |
| Minister | ***Provides assurance*** |
|  |  |
| Internal audit | ***Provides some assurance*** |
|  |  |
| Audit committee | ***Provides assurance*** |

Senior management

1. Although the position of Head of Trading Entity has been filled, and senior positions in Finance division are no longer vacant, there remains a concern over a lack of certainty in some senior management positions in certain critical operational directorates. As a result, limited assurance has been provided by senior management of the entity.

Accounting officer

1. The accounting officer has put initiatives in place to provide assurance. These initiatives are monitored regularly and management is held accountable where weaknesses are identified. Some of the interventions did not take place timeously, and as a result the required improvements in audit outcome has not yet realised.

Minister

1. The ‘turnaround’ strategy has been a key focus area during the Minister’s term in office. The interventions put in place did not, however, have the desired impact in the current financial period.

Internal audit

1. Legislation in South Africa requires the establishment and roles and responsibilities of internal audit units. Internal audit units form part of the internal control and governance structures of the entity and play an important role in its monitoring activities. Internal audit provides an independent assessment of the entity’s governance, risk management and internal control processes.
2. The internal audit unit of a trading entity must prepare a risk-based audit plan and internal audit programme for each financial year. It must advise the accounting officer and report to the audit committee on implementing the internal audit plan and matters relating to internal audit; internal controls; accounting procedures and practices; risk and risk management; performance management; loss control and compliance with the PFMA. The internal audit unit must also perform such other duties as may be assigned by the accounting officer.
3. The internal audit function was still under-capacitated during the period under review considering the size of and risk relating to the department and the PMTE. Internal audit is responsible for normal internal audits as well as the investigation of allegations of misconduct in terms of their internal audit and investigation service charter. With regard to the latter, capacity in the form of private service providers has been in-sourced.

Audit committee

1. The audit committee is an independent advisory body to the accounting officer and the management and staff of the trading entity on matters relating to internal financial control and internal audits; risk management; accounting policies; the adequacy, reliability and accuracy of financial reporting and information; performance management; effective governance; the DoRA, PFMA, Treasury Regulations and any other applicable legislation; performance evaluation; and any other issues.
2. As mention above, the audit committee is currently effectively involved from a governance perspective in the department and entity’s turnaround process, which is an on-going project

Status of implementing commitments and recommendations

1. Below is our assessment of the progress in implementing the commitments made by the trading entity to address the prior and current year’s audit findings.

| **No.** | **Commitment** | **Made by** | **Date** | **Status** |
| --- | --- | --- | --- | --- |
| 1. **Commitments made by minister** | | | | |
| 1.1. | Focus will be placed on changing management style and creating a stronger control environment within the Department and PMTE | Hon. T Nxesi (Minister of Public Works) | 09-Sep-14 | In progress |
| 1.2. | The Minister committed to investing in adequate and sufficiently skilled resources, as well as adequate IT systems, in order to properly capacitate the Department and PMTE. | Hon. T Nxesi (Minister of Public Works) | 09-Sep-14 | Intervention required.  While cognisance is taken of the fact that appointments have been made in the Finance department, the new accounting system that has been procured has still not been adequately implemented to assist management in addressing the findings of previous years. Significant balances and transactions of the entity were still compiled outside of the SAGE system for the period under review. |
| **Commitments made by accounting officer to address audit qualification matters** | | | | |
| **2. Lease portfolio management** | | | | |
| 2.1. | The design and implementation of business processes and IT systems that will ensure the efficient and effective management of the leases portfolio. | Mr M Dlabantu | 26-Mar-14 | In progress.  Progress has been noted insofar as no significant errors were noted in calculations for accounting purposes.  The focus of management should now be on ensuring that amounts paid to landlords are as per lease agreements, as over and underpayments are still being made. |
| **3. Supply chain management** | | | | |
| 3.1. | The department commit to clear irregular expenditure and non-compliant expenditure by developing relevant policies and procedures, enhancing the monitoring, enforcing compliance and holding officials accountable. | Mr M Dlabantu | 26-Mar-14 | In progress  Irregular expenditure was identified during the current period. |
| 3.2 | Records management will also be improved to enable proper audit trail. | Mr M Dlabantu | 26-Mar-14 | In progress. A new records management system has been procured. The planned date for initial implementation was 2015/16, however as at year end the full benefit has not been realised.. |
| 3.3 | Capacity will be created at Head Office and Regional level in line with revised organizational structure | Mr M Dlabantu | 26-Mar-14 | Capacity with the required skills remained a challenge, especially at regional level.. |
| 3.4 | Training will be provided to all SCM officials. | Mr M Dlabantu | 26-Mar-14 | In progress, training was provided. It is however a concern that there was not a noticeable improvement in SCM compliance, therefore casting a doubt on the effectiveness of the training. . |
| **4. Financial management** | | | | |
| 4.1 | The department commits to improving the financial management by conducting monthly reconciliations, managing the commitments, contingent liabilities and assets, and accruals better. | Mr M Dlabantu | 26-Mar-14 | Intervention required.  The audit qualifications from the prior period have not been adequately resolved, and significant matters were identified in the current period relating to commitments, contingent liabilities and assets, and accruals. |
| **5. IT controls** | | | | |
| 5.1 | An IT master plan to be developed. | Mr M Dlabantu | 26-Mar-14 | In progress.  The new billing and accounting system (SAGE) has been procured. It is however a concern that only the modules relating to payments and receipts have been implemented, especially considering that it has been more than a year since the system was procured.  ICT Governance framework has been developed and signed into effect by the DG. The entity must prioritise the appointment of sufficient appropriately skilled ICT staff to enable effective implementation of the ICT governance framework. It is of significant concern that senior positions within the ICT section are being occupied by consultants. |
| **6. Human resource management** | | | | |
|  | The filling of vacant posts is on-going and strictly monitored | Mr M Dlabantu | 26-Mar-14 | In progress.  Appointments were made during the period, however this cannot be properly assessed as the proposed new structure is yet to be approved. |
| **7. Governance** | | | | |
|  | To entrench the principle of accountability, the department has established the Accountability Management Committee as a forum for all senior managers to report on their areas of responsibility and corrective measures taken where required. | Mr M Dlabantu | 26-Mar-14 | In progress.  The Committee has been established, however significant work is still required with regards to consequence management as investigations are not finalised timeously |
|  | The Governance, Risk and Compliance management is being elevated to a Branch level and will be capacitated to enable improved risk management for all operations. | Mr M Dlabantu | 26-Mar-14 | In progress.  The Committee has been established, however significant work is still required with regards to consequence management |
| **8. Asset management** | | | | |
|  | A comprehensive action plan to ensure the development of a fully compliant immovable asset register in line with the GRAP requirements is being implemented. | Mr M Dlabantu | 26-Mar-14 | Intervention required.  The process of initially accounting for the immovable assets acquired through the transfer of functions was not adequately completed prior to the end of the financial year under review. Significant weaknesses were identified in the model utilised by the entity to account for immovable assets in line with the requirements of GRAP. |
|  | The on-going improvements of the movable asset register following the transfer of functions and the operationalization of the PMTE. | Mr M Dlabantu | 26-Mar-14 | Complete.  The identification of all the movable assets was finalised as at the reporting date, and no major issues were identified in this regard. |
| **9. Compliance** | | | | |
|  | The department will review, align, communicate and ensure implementation of all the operational and financial management policies. | Mr M Dlabantu | 26-Mar-14 | In progress, significant progress was made in developing and approving policies throughout the period. Various instances of non-compliance has been identified as reported under section 2 part D, |

1. Details on the status of implementing the previous year(s) recommendations are provided in section 8, which summarises the detailed audit findings.

**2.7 OTHER REPORTS**

1. I draw attention to the following engagements that could potentially have an impact on the trading entity’s financial-, performance- and compliance-related matters. My opinion is not modified in respect of these engagements that are either in progress or have been completed.

Investigations

1. Numerous allegations, mainly relating to transgressions with respect to supply chain management, potential fraud and financial misconduct, are still being investigated on an ongoing basis by the SIU and the Governance, Risk and Compliance unit of the department

**SECTION 3: Specific focus areas**

**3.1 FINANCIAL VIABILITY**

1. Our audit included a high-level overview of the trading entity’s financial viability as at year-end. The financial viability assessment provides useful information for accountability and decision-making purposes and complements the financial statements by providing insights and perspectives thereon. The financial viability assessment is expected to enhance timely remedial decision-making and policy reforms where financial viability may be at risk. It will also highlight to management those issues that may require corrective action and the urgency and magnitude of the reforms and decisions necessary to maintain operations. The information should be used to complement, rather than substitute, management’s own financial assessment.

| **FINANCIAL VIABILITY ASSESSMENT** | | | |
| --- | --- | --- | --- |
| **(Limitation = unable to obtain sufficient appropriate information to assess the indicator)** | | **AS AT 31 MARCH 2016** | **AS AT 31 MARCH 2015** |
| **EXPENDITURE MANAGEMENT** | | | |
| 1.1 | Creditor-payment period | **177 Days** | **197.9 Days** |
| **REVENUE MANAGEMENT** | | | |
| 2.1 | Debtor-collection period (after impairment) | **68.1 Days** | **22.1 Days** |
| 2.2 | Debtors impairment provision as a percentage of accounts receivable | **39.1%** | **70.2%** |
| * Amount of debtors impairment provision * Amount of accounts receivable | **R1 546 094**  **R3 954 670** | **R1 779 050**  **R2 535 951** |
| **ASSET AND LIABILITY MANAGEMENT** | | | |
| 3.1 | A deficit for the year was realised (total expenditure exceeded total revenue) | **Yes** | **No** |
| * Amount of the surplus / (deficit) for the year | **R766 429** | **R744 635** |
| 3.2 | A net current liability position was realised (total current liabilities exceeded total current assets) | **Yes** | **Yes** |
| * Amount of the net current assets / (liability) position | **(R7 969 395)** | **(R5 768 155)** |
| 3.3 | A net liability position was realised (total liabilities exceeded total assets) | **No** | **No** |
| * Amount of the net asset / (liability) position | **R104 428 416** | **R123 539 334** |
| 3.4 | Liquid assets as a percentage of total current liabilities (acid test percentage) | **-29.1%** | **-30.0%** |
| * Amount of liquid assets (total current assets less inventory less prepayments) * Amount of total current liabilities | **R3 639 739**  **R12 514 662** | **R2 739 174**  **R9 134 040** |
| **CASH MANAGEMENT** | | | |
| 4.1 | The year-end bank balance was in overdraft | **Yes** | **Yes** |
| * Amount of year-end bank balance (cash and cash equivalents) / (bank overdraft) | **(R1 473 588)** | **(R661 391)** |
| 4.2 | Net cash flows for the year from operating activities were negative | **No** | **No** |
| * Amount of net cash in / (out)flows for the year from operating activities | **R3 822 503** | **R3 218 560** |
| 4.3 | Creditors as a percentage of cash and cash equivalents | **Bank in overdraft** | **Bank in overdraft** |
| * Amount of creditors (accounts payable) * Amount of cash and cash equivalents / (bank overdraft) at year-end | **R3 821 069**  **(R1 473 588)** | **R3 661 677**  **(R661 391)** |
| **OVERALL ASSESSMENT** | | | |
| Overall the financial viability is assessed as: | | **Yellow (Concerning)** | **Yellow (Concerning)** |
| *\* These amounts have been adjusted for uncorrected misstatements that resulted in the modification of the audit opinion and will therefore not agree to the financial statement amounts. [[1]](#footnote-1)* | | | |

1. The entity’s overdraft has increased from R661 million in 2015 to R1 473 million at year-end. In addition, the net current liability situation has deteriorated, with current liabilities exceeding current assets by R7.9 billion (2015: 5.7 billion). However, the entity is now comfortably in a net asset position. The overall financial situation of PMTE can be summarised as being unfavourable but improving

**3.2 PROCUREMENT AND CONTRACT MANAGEMENT**

1. The audit included an assessment of procurement processes, contract management and the related controls in place. To ensure a fair, equitable, transparent, competitive and cost-effective supply chain management (SCM) system, the processes and controls need to comply with legislation and minimise the likelihood of fraud, corruption, favouritism and unfair and irregular practices.
2. A summary of the findings from the audit are as follows:

Irregular expenditure

1. R 587 264 465 (100%) of irregular expenditure incurred in the current financial year was as a result of the contravention of SCM legislation. Thirteen percent of this irregular expenditure was identified during the audit process and not detected by the entity monitoring processes. The root cause of the lack of effective prevention and detection are officials contravening the SCM regulation.

Awards to persons in the service of the state and their close family members

1. The audit included an assessment of the interests of officials and their close family members in suppliers to the trading entity. Legislation does not prohibit such awards, but compliance with the legislation and policies was tested to ensure that conflicts of interest did not result in contracts being unfairly awarded or unfavourable price quotations being accepted, and that employees obtained approval for performing remunerative work outside their employment as required.

The findings were as follows (the regions are in the process of consolidation and not all regions are included in the table below):

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Finding** | **Number and value of awards made** | **Number and positions of official identified** | **Number of suppliers identified** | **Further non-compliance or irregularities regarding the awards** | | | |
| **Supplier did not submit declarations of interest** | **Supplier did not declare interest (false declaration)** | **Official did not declare interest** | **Official was involved in awarding the contract/ quotation** |
| Awards made to officials of the trading entity | - | - | - | - | - | - | - |
| Awards made to close family members, partners and associates of officials of the trading entity | 26  R48 820 207 | 26 | 26 | 1 | 6 | 2 | - |
| Awards to persons in the service of other state institutions | - | - | - |  |  |  | - |

Procurement processes

1. The table below is a summary of findings identified on procurement processes (the regions are in the process of consolidation and not all regions are included in the table below):

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Total | | Quotations | | Contracts | |
| Number | Value | Number | Value | Number | Value |
| **Awards selected for testing** | *128* | *R4 993 452 229* | *61* | *R14 066 743* | *67* | R4 979 385 486 |
| **Expenditure incurred on selected awards - current year** |  | *R1 158 512 360* |  | *R12 499 191* |  | *R1 146 013 169* |
| **Limitations - awards selected but could not be tested** | *4* | *R322 742 469* | *1* | *R69 301* | *3* | *R322 673 168* |
| **Awards on which non-compliance was identified** | *51* | *R3 081 474 741* | *20* | *R5 031 796* | *31* | *R3 076 442 945* |
| **Irregular expenditure identified** | *35* | *R1 221 268 092* | *15* | *R3 597 849* | *20* | *R1 217 670 243* |
| **Instances of irregular expenditure where goods/ services were not received** | *-* | *-* | *-* | *-* | *-* | *-* |

**Limitations on audit**

1. As indicated in the table above, sufficient appropriate audit evidence could not be provided that four of selected awards to the value of R322 742 469 were made in accordance with the requirements of applicable SCM legislation. No alternative audit procedures could be performed to obtain reasonable assurance that the expenditure incurred on these awards was not irregular.

The reasons for the limitations were improper record keeping. As a result of these limitations, the findings reported in the rest of this section may not reflect the true extent of irregularities and SCM weaknesses.

**Procurement processes – general**

1. One major projects to the value of R30 443 000 were procured without a proper needs assessment being conducted in the form of a project evaluation.
2. Three awards to the value of R814 091 were procured without inviting at least the minimum prescribed number of written price quotations from prospective suppliers and the deviation was not approved by a properly delegated official.
3. Eleven awards with a value of R4 254 881 were procured without inviting at least the minimum prescribed number of written price quotations from prospective suppliers, and the deviation was approved even though it was possible to obtain the quotations.
4. Nineteen contracts and/or quotations to the value of R890 971 789 were procured from suppliers whose tax matters had not been declared by the South African Revenue Services to be in order.
5. Eight contracts with a value of R834 821 258 were procured without inviting competitive bids, and the deviations were not approved.
6. Three contracts with a value of R84 962 595 were procured without inviting competitive bids, and the deviations were approved even though it was practical to invite competitive bids.
7. Invitations for competitive bids for the procurement of two contracts with a value of R71 762 499 were not advertised for the required minimum number of days.
8. Nine contracts with a value of R888 758 293 were awarded to bidders who did not submit a declaration of past supply chain practices such as fraud, abuse of the SCM system and non-performance.
9. Five contracts and/or quotations to the value of R925 219 777 were awarded based on criteria that differs from the original specifications.
10. Seven contracts were awarded to bidders based on preference points that were not allocated and/or calculated according to the requirements of the Preferential Procurement Policy Framework Act and its regulations.
11. One contract was awarded to bidders who did not score the highest points in the bid evaluations, and there was no justification for the deviation.
12. Twelve contracts and/or quotations were awarded to bidders who did not submit a declaration of whether they were employed by the state or connected to any person employed by the state.

*Construction contracts*

1. One construction contract with a total value of R155 786 000 were awarded to contractors whose CIDB grading is below the required grading for the value of the particular contract

**Contract management**

1. Three contracts were amended or extended without approval by a delegated official. The total value of the extensions is R6 129 367
2. The contract performance and monitoring measures and methods applied in monitoring two contracts with a total value of R34 501 143 were insufficient to ensure effective contract management.

Internal control deficiencies

1. The following internal control deficiencies should be addressed to improve procurement and contract management at the trading entity:

* Lack of proper procurement planning which resulted in numerous deviations from the procurement process.
* Internal investigations were not being started and finalised within the prescribed time frames. This was mostly due to large volume of allegations and lack of capacity. This has a negative impact on being able to enforce appropriate disciplinary action in a timeous manner.
* The accounting officer did not in some instances exercise oversight responsibility of reporting and compliance with laws and regulations and internal control.

1. Reviewing and monitoring of compliance with applicable laws and regulations was insufficient and not properly monitored.

**3.3 FRAUD AND CONSEQUENCE MANAGEMENT**

1. The primary responsibility for preventing and detecting fraud rests with management and those charged with governance. We are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error, and to issue an auditor’s report that includes our opinion. Due to the inherent limitations of an audit, there is a risk that some material misstatements, including fraud, may not be detected.
2. Below is a summary of fraud risk factors that should be addressed to ensure that sufficient measures/controls are in place to prevent material misstatement due to fraud.

* The entity did not have systems in place to assist in the preparation of financial statements on the accrued basis of accounting throughout the year. At present all transactions are being recorded on the cash basis of accounting, resulting in material journals being processed manually at year-end. This is highly susceptible to human error.
* Significant management estimates are required for financial statement amounts for provisions and the calculation for impairment for debtors.

1. The PFMA and its regulations clearly stipulate that matters such as incurring unauthorised, irregular as well as fruitless and wasteful expenditure; the possible abuse of the SCM system (including fraud and improper conduct); and allegations of financial misconduct should be investigated. Disciplinary steps should be taken based on the results of the investigations. Our audits included an assessment of the trading entity’s management of consequences. The significant findings are provided below:

Inadequate measures to manage consequences

1. The statistics in the table below indicate the effectiveness of the department’s measures for responding to allegations of financial misconduct, fraud and other improper conduct in SCM.

|  |  |  |
| --- | --- | --- |
|  | **Allegations reported in the prior year** | **Allegations reported in the current year** |
| Number of cases of fraud/corruption reported through the auditee's internal mechanism | 313 | 41 |
| Number of cases investigated (in relation to number of cases reported) | 263 | 28 |
| Number of cases not yet investigated (in relation to number of cases reported.) | 50 | 0 |
| Number of investigations finalised i.e. report issued | 208 | 6 |
| Number of cases that resulted in disciplinary actions, civil recoveries or criminal charges being laid | 0 | 0 |
| Number of cases that have been referred to the law enforcement/investigation agencies *e.g. the SAPS, the Public Protector, the Competition Commission, or the SIU* | 29 | 13 |

Failure to implement consequences

1. The table below provides a summary of transgressions from the previous year that were either not investigated or proper disciplinary steps were not taken after investigation.

**Irregular and fruitless and wasteful expenditure**

| Finding | Value |
| --- | --- |
| Irregular expenditure identified in the previous year was not investigated to determine if a person was liable for the expenditure. | 31 985 176 223 |
| Fruitless and wasteful expenditure identified in the previous year was not investigated to determine whether a person was liable for the expenditure | 261 413 727 |

**Transgressions identified in the current year**

1. Irregular and fruitless and wasteful expenditure disclosed in note 30 and 31 to the financial statements must be investigated to determine whether any official is liable for losses incurred as a result of the irregular/fruitless and wasteful expenditure. Disciplinary steps must be taken against officials who caused or permitted the Irregular and fruitless and wasteful expenditure and losses incurred as a result must be recovered from the person liable.
2. This report includes other audit findings that are indicative of transgressions by officials or other role players. Summarised in the table below are allegations of transgressions that must be investigated and disciplinary steps taken based on the results of the investigations:

| Finding | Number of instances | Value |
| --- | --- | --- |
| Official failed to disclose their own interest or that of close family members, partners or associates in contracts | 3 | 110 427 023 |
| Supplier submitted false declaration of interest | 13 | 117 538 889 |
| Possible performance of additional remunerative work without approval | 28 | 45 904 940 |
| Lack of delivery or poor performance by the contractor | 28 | 302 750 747 |

**SECTION 4: Emerging risks**

**Accounting, performance management/reporting and compliance matters**

**Standards of GRAP**

1. Amendments to the following standards of GRAP will become effective for financial periods commencing on or after 1 April 2016:

* *GRAP 16 – Investment property*
* *GRAP 17 – Property, plant and equipment*

*GRAP 12 – Selection of an appropriate reporting framework by public entities* becomes effective for financial periods commencing on or after 1 April 2018.

1. The ASB has issued the following additional standards of GRAP for which effective dates have not yet been gazetted by the minister of Finance:

* *GRAP 20 – Related party disclosures*
* *GRAP 32 – Service concession arrangements: grantor*
* *GRAP 108 – Statutory receivables*
* *GRAP 109 – Accounting by principals and agents*

New legislation

**Treasury Regulations**

1. The Treasury Regulations are currently being revised, which may introduce a number of new requirements once effective.

**Central Supplier Database:**

1. The OCPO introduced the Central Supplier Database on 1 September 2015 accessible on [www.csd.gov.za](http://www.csd.gov.za), which will reduce the administrative burden on both the supplier and the administrator. The system verifies and validates information with the South Africa Revenue Service (SARS), Companies and Intellectual Property Commission (CIPC), and Department of Home Affairs amongst others. The system will be mandatory from 1 April 2016 for all suppliers to national and provincial government and entities at these two spheres of government. It will be rolled out to local government from 1 July 2016.

**eTenders Portal:**

1. Suppliers who meet all compliance requirements can access opportunities on [www.eTenders.gov.za](http://www.eTenders.gov.za). The portal enables suppliers to have access to tenders published on the platform. The compulsory implementation of this portal is from 1 April 2016.03.29

**SECTION 6: Ratings of detailed audit findings**

1. For the purposes of this report, the detailed audit findings included in annexures A to C have been classified as follows:

* Matters to be included in the auditor’s report: These matters should be addressed as a matter of urgency.
* Other important matters: These matters should be addressed to prevent them from leading to material misstatements of the financial statements or material findings on the performance report and compliance with legislation in future.
* Administrative matters: These matters are unlikely to result in material misstatements of the financial statements or material findings on the performance report and compliance with legislation.

**SECTION 7: Conclusion**

1. The matters communicated throughout this report relate to the three fundamentals of internal control that should be addressed to achieve sustained clean administration. Our staff remains committed to assisting in identifying and communicating good practices to improve governance and accountability and to build public confidence in government’s ability to account for public resources in a transparent manner.

Yours faithfully

Corne Myburgh

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31 July 2016

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**Distribution:**

Audit committee

Head of internal audit unit

1. The auditor should indicate which of the R-amounts included in the financial viability table have been adjusted for uncorrected misstatements that resulted in the modification of the audit opinion by placing an asterisk (\*) next to such amounts. [↑](#footnote-ref-1)