PREVENTATIVE
CONTROL GUIDES

AUDITOR-GENERAL
SOUTH AFRICA

GUIDES 1 - 7

AUDITOR-GENERAL'S FOREWORD

Congratulatory Greetings,

I have the immense pleasure and honour to commend you and convey my warmest congratulations and best wishes to you on your appointment as leaders of the 7th Administration of the Republic of South Africa. May your tenure be marked with accountability, good governance and progress for the betterment of all.

As a chapter 9 institution with a constitutional mandate to strengthen democracy by auditing government spending, the Auditor-General South Africa (AGSA) strives to provide you with tools and insight that will empower you to achieve your mandates.

One such a tool is the **Preventative control guide,** which is part of a series of guides on preventative controls and a system of accountability.

Internal controls are categorised as preventative controls, detective controls and corrective controls. Preventative controls are the controls designed and implemented by management to avoid threats to the objectives of the institution materialising. Detective and corrective controls focus more on identifying and correcting failures after they had already occurred.

Preventing poor-quality financial statements and performance reports, and non-compliance and material irregularities, is more effective and efficient than having to deal with their consequences – money and time is lost, investigations are costly and officials are subjected to the discomfort and anxieties associated with these processes, which at times take months and years to bring to finality.

The amended Public Audit Act (PAA) empowered the auditor-general to issue material irregularities (MI), refer matters to a relevant public body for investigation, to take appropriate legally binding remedial action and/or to issue a certificate of debt where the accounting officer or accounting authority failed to comply with the remedial action.

The AGSA's message has been consistent over the years: strong control environments and processes are key to achieving objectives, addressing risks, ensuring compliance with legislation, and managing public sector funds for the benefit of citizens. Accounting officers and authorities have a legislated obligation to implement and maintain effective, efficient and transparent systems of financial and risk management, and internal control. Oversight structures and executive authorities should hold the accounting officers and authorities accountable (AO/AA) for the effectiveness of the internal controls.

Preventive controls should be designed, implemented and work effectively in all the key processes to identify failures that could threaten the finances, performance, delivery and accountability processes. A preventative control can be in place, but for it to work effectively, in the right way, at the right time and every time, it must be built in a strong control environment. This includes a leadership tone and culture in the institution that supports the need for controls as well as institutionalised internal controls at an organisational level. Obtaining and providing assurance that the controls are in place and working effectively should be a key priority.

We developed these guides to assist and empower accounting officers and accounting authorities to invest in preventative controls in order to stem the tide of misappropriation of funds. They have relevant information for all roleplayers in the accountability ecosystem. In essence, if properly designed and implemented, preventative controls are an invincible fortress against all possible abuses of the public purse which will inevitably re-establish accountability as a cornerstone of our democracy. Once controls are in place and are diligently pursued, there will be more resources available to meet the obligations of the allocated budget towards its democratic mandate of improving the quality of lived experiences of citizens.

The National Treasury had an amicable agreement with the AGSA whereby the former director-general, Dondo Mogajane, noted: "These guides on preventative controls will add to our arsenal of measures to safeguard public money and rid our public sector of the scourge of malfeasance."

And so, as we usher in the appointed leadership of South Africa's 7th Administration, we undertake to collaborate with you to shift the culture of the public sector by introducing you to the tools that will, with a strong tone at the top, an ethical culture, integrity, performance measures and transparency set a concrete foundation for good governance. Where you implement preventative controls with diligence, they become a natural source of consequences.

> These guides on preventative controls will add to our arsenal of measures to **safeguard public money** and rid our public sector of the scourge of malfeasance.

I wish to appeal to all roleplayers entrusted with various responsibilities in the accountability ecosystem to effectively play your part and do everything within your mandates to safeguard public funds which are already struggling to meet demand.

I extend gratitude to all of you for your contribution to managing public resources and acknowledging the importance of the National Treasury and the AGSA working shoulder to shoulder in our relentless pursuit of good public sector financial management and accountability.

Tsakani Maluleke
Auditor-General

The AGSA's message has been consistent over the years: strong control environments and processes are key to achieving objectives.

AUDITOR-GENERAL
SOUTH AFRICA

PREVENTATIVE
CONTROL GUIDES

GUIDES 1-3

INTRODUCTION & ORGANISATIONAL LEVEL

IMPORTANCE OF PREVENTATIVE CONTROLS

GUIDE 01

What this guide is about

The system of accountability has reached a point where government must invest in preventative controls. This guide is the first in a series on preventative controls. It describes the aim of the guides and introduces them by explaining some key concepts.

Preventative controls

The AGSA's message has been consistent over the years that a strong control environment and processes are the key to achieving objectives, addressing risks, ensuring compliance with legislation, and managing public sector funds to the benefit of citizens.

Accounting officers and authorities (AO/AA) have a legislated obligation as defined in the Public Finance Management Act (PFMA) and the Municipal Finance Management Act (MFMA) to implement and maintain effective, efficient and transparent systems of financial and risk management and internal control. Oversight structures and executive authorities should keep the AO/AA accountable for the effectiveness of the internal controls.

Internal controls can be categorised as preventative controls, detective controls and corrective controls. Preventative controls are the controls designed and implemented by management to avoid threats to the objectives of the institution materialising. Detective and corrective controls focus more on identifying and correcting failures after they had already occurred.

Preventing poor-quality financial statements and performance reports, non-compliance and material irregularities is more effective and efficient than having to deal with the consequences thereof – money and time are lost, costly investigations have to be instituted, and officials are subjected to the discomfort and anxieties associated with these processes, which often take a number of years to be finalised.

Preventive controls should be designed, implemented and working effectively in all the key processes of an institution. This will give comfort to the AO/AA, executive authority and oversight structures that any failures that could threaten the finances, performance, delivery and accountability processes of their institution will be prevented.

A preventative control can be in place, but for it to work effectively (in other words, in the right way, at the right time, every time) it must be built on a strong control environment. This includes a leadership tone and culture in the institution that supports the need for controls as well as institutionalised internal controls at organisational level. Obtaining and providing assurance that the controls are in place and working effectively should be a key priority of the AO/AA and senior managers.

The diagram that follows illustrates these concepts.

TYPICAL BUSINESS PROCESSES OF THE INSTITUTION

- SUPPLY CHAIN MANAGEMENT
- CONTRACT MANAGEMENT
- PAYMENT
- EMPLOYEE PROCESSES AND PAYROLL
- ASSET AND LIABILITY MANAGEMENT
- REVENUE MANAGEMENT

PREVENTATIVE CONTROLS

Built on **strong control** environment with assurance provided by:

- SENIOR MANAGEMENT
- ACCOUNTING OFFICER/ AUTHORITY
- INTERNAL AUDIT UNIT AND AUDIT COMMITTEE

Preventative controls not designed or implemented or not working effectively

MATERIAL IRREGULARITIES AND POOR AUDIT OUTCOMES

CONSEQUENCES

- FINANCIAL LOSS
- COSTLY INVESTIGATION
- DISCIPLINARY PROCESSES
- LITIGATION

01

Where to start

It takes time to institutionalise good preventative controls, especially in large and complex environments, but the AO/AA need to build their institutions towards accomplishing this is in deliberate manner.

They should identify the areas of greatest risk in their institutions and focus on strengthening those areas first with preventative controls – by applying the 80:20 rule, the greatest impact can be achieved through the lowest effort by focusing on the 20% that will bring 80% of the results. Oversight structures should also focus their efforts towards obtaining assurance that preventative controls are in place in these areas of greatest risk to the institutions.

Why these guides

The general report on the 2018-19 audit outcomes of national and provincial government was tabled in November 2019 with a strong message that good preventative controls should be institutionalised in a deliberate and focused manner.

The message was well received by oversight structures and executive authorities, and the need for the AGSA to support this new administration in their commitment to focus on prevention was apparent. The overall aim of these guides is thus to support this new chapter in the accountability journey.

The objectives of these guides are to:

- Enable oversight structures to assess whether the most important preventative controls are implemented by institutions to address their main areas of risks. This will assist oversight structures to diagnose weaknesses in preventative mechanisms and focus their oversight efforts on obtaining assurance from the executive authority and the AO/AA that those weaknesses are being effectively addressed in accordance with their legislated obligations.
- Enable the AO/AA and the executive authority to effectively address the assurance needs of oversight structures pertaining to preventative controls.
- Create general awareness of the role of the AO/AA and their legislated obligations towards good financial and performance management in their institutions.

01

What we will provide

Guides on preventative controls will be published covering the following categories:

1. The control environment as a basis for all preventative controls, presented within two broad categories:
   - Tone and control culture – dealing with controls that should be in place at an organisational level to enable an ethical and effective control culture, including leadership effectiveness and conduct.
   - Institutionalised internal controls – dealing with controls that should be in place at an organisational level to enable the implementation and monitoring of, and the assurance on, preventative controls.
2. Transactional level controls – dealing with controls within the key business processes of institutions, such as procurement, payments, financial statement preparation, and asset management.
3. Project management and delivery controls – dealing with key delivery areas, including infrastructure development and maintenance.

The guides cover the main preventative controls that should be in place and include key questions that oversight structures and executive authorities can ask to obtain assurance on whether the controls have been implemented and are working effectively. In each guide, this is presented as questions to ask the AO/AA.

The preventative control guides are available on the AGSA's website (www.agsa.co.za).

What this guide is about

Preventative controls are measures built into the processes of an institution at transactional level to prevent errors, fraud or any failure to achieve specific objectives.

A preventative control can be in place, but for it to work effectively (in other words, in the right way, at the right time, every time) it must be built on a strong control environment.

The control environment is the set of standards, processes and structures that provides a basis for carrying out internal control across the institution.

A key element of this control environment is an ethical and effective control culture at the institution. Leadership sets the tone at the top. If an institution's leaders are unethical; have a disregard for governance, compliance and control; and are not committed to transparency and accountability, it will filter through to the lower levels.

Inevitably, a culture of poor discipline and impunity will develop – a culture in which preventative controls will not be effective.

This guide deals with the tone and culture controls that should be in place at institutions as the foundation for preventative controls.

Oversight structures and executive authorities can use this guide to require assurance from accounting officers and authorities (AO/AA) that these controls have been implemented and are working effectively – this is presented as questions to ask the AO/AA.

Controls accounting officers and authorities should implement

A commitment to integrity and ethical values is demonstrated through:

- The tone at the top – Through their directives, actions and behaviour, the AO/AA and management at all levels should demonstrate the importance of integrity and ethical values to support the functioning of the system of internal control.
- Established standards of conduct – The expectations of the AO/AA and senior management concerning integrity and ethical values should be defined in the institution's standards of conduct and understood at all levels of the organisation. For most public sector institutions, the basis for any standards of conduct is included in legislation.
- Evaluating adherence to standards of conduct – Processes should be in place to evaluate the performance of individuals and teams against the expected standards of conduct.
- Addressing deviations in a timely manner – Deviations from the expected standards of conduct should be identified and remedied in a timely and consistent manner.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Is a formal code of conduct in place and does it clearly set out expected standards of ethical and moral behaviour to all officials? What was the basis for the code?
2. How is it ensured that all officials are aware of, and have committed to, this code?
3. How is officials' adherence to the code of conduct evaluated?
4. If deviations from the code of conduct are identified, what processes are in place to address this appropriately and in a timely and consistent manner?
5. Provide reports on the transgressions identified in the past year, how these were addressed and how similar instances can be prevented in future.

Why it is important

Even if an institution has very good internal controls, it can be circumvented if those responsible for implementation and enforcement choose to do so. Such behaviour can be as a result of negligence or a wilful act for personal gain. Being clear on what the expected conduct of all officials in line with the ethical values of the institution should be, and evaluating and enforcing such conduct, demonstrate the commitment by leadership to integrity and ethical values.

But even such commitment can be overshadowed by leadership's own behaviour – unethical behaviour that is in sharp contrast with the code of conduct of the institution will inevitably result in such behaviour being echoed across the institution.

Applicable legislation

Section 195(1)(a) of the Constitution of the Republic of South Africa prescribes that a high standard of professional ethics must be promoted and maintained.

The Public Service Regulations describe the code of conduct expected from public officials and the management of ethics in parts 1 and 3 of chapter 2, respectively.

Section 50(1)(b) of the Public Finance Management Act (PFMA) stipulates that the accounting authority for a public entity must act with fidelity, honesty, integrity and in the best interest of the public entity in managing the financial affairs of the public entity.

Schedule 2 of the Municipal Systems Act describes the code of conduct for municipal staff members.

Controls accounting officers and authorities should implement

Independent oversight is provided through:

- Performing oversight of the development and performance of internal control and raising difficult questions and pursuing answers from management where applicable.
- Regularly engaging with the internal audit unit and the external auditors (AGSA), the chair of the audit committee, and others as appropriate, to discuss the effectiveness of internal control over financial reporting, performance reporting and compliance with legislation.
- Taking appropriate actions to ensure that identified deficiencies in internal control are addressed by management on a timely basis.
- Demonstrating a positive attitude towards accountability through credible financial and performance reporting and for the rule of law.
- Demonstrating independence from the institution and objectivity in its oversight.

Questions oversight structures and executive authorities could ask to obtain assurance

1. What is the view of the AO/AA on why internal control, accountability and compliance with legislation are important for the institution to succeed? Why should the institution produce credible financial and performance reports?
2. How do the AO/AA oversee the implementation and monitoring of internal controls? What information is reported by management on the status of internal control and how often? What do the AO/AA do with the information – what questions are asked and how do the AO/AA satisfy themselves of the integrity of the answers provided?
3. How often do the AO/AA engage with the internal audit unit, the external auditors (AGSA) and the chair of the audit committee on the effectiveness of internal control over financial reporting, performance reporting and compliance with legislation? What is typically the outcome of such engagements?
4. If deficiencies in internal control are identified (e.g. by auditors or management), what steps are taken by the AO/AA to ensure that these are addressed?
5. Are the AO/AA independent from the institution? How is objectivity in oversight enabled?
6. What internal control deficiencies in the institution are currently the main focus of the AO/AA? How were these identified and how will the AO/AA through their oversight address the deficiencies?

Why it is important

The AO/AA take overall responsibility for the financial management of an institution and the achievement of its objectives. The actions, directives and focus of the AO/AA set the tone for the institution.

If the importance of internal controls and accountability is not accentuated at this level, there will be little commitment and discipline towards it in the institution.

Applicable legislation

Section 38(1)(a)(i) of the PFMA states that the accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 51(1)(a)(i) of the PFMA prescribes that an accounting authority of a public entity must ensure that the public entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 62(1)(c)(i) of the Municipal Finance Management Act (MFMA) specifies that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Controls accounting officers and authorities should implement

The discipline of adherence to controls on a daily basis should be ingrained into the culture of the institution.

Officials should know, accept and embrace their responsibilities towards controls; understand how to execute the control activities; and be enabled through standardised processes, checklists, templates, reports, automation, etc. to execute these activities at the right time, in the right way, every time.

Officials should be enabled and encouraged to raise the alarm if controls are being circumvented.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Is there a strong control culture in the institution? Provide motivations for the answer.
2. How has it been ensured that all officials in the institution understand their responsibility toward controls and what is expected from them in this regard on a day-to-day basis? Do their job descriptions include this? Is it included in their performance contracts? [The question can be asked for all officials or for a specific group, e.g. senior management, the finance unit, or supply chain management officials.]
3. Do officials receive training, manuals or communication explaining how to execute the control activities? Are all processes and required control activities documented? What is in place to help officials execute the control activities at the right time, in the right way, every time? [The question can be asked for all officials or for a specific group, e.g. senior management, the finance unit, or supply chain management officials.]
4. Is a mechanism in place for officials to report the circumvention of controls in a manner that safeguards the official? How are officials encouraged to use such a mechanism? Provide reports on the type of incidents reported in the past year and how these are being dealt with.
5. If it was found (by the external auditors (AGSA), internal audit unit or another institution) that there are significant control deficiencies in a process of the institution:
   a. Were specific officials responsible for the execution of the control?
   b. How were these officials enabled by the institution to execute the control?
   c. What is the reason for the officials not executing their control activities or not executing them timeously/correctly?
   d. What actions are being taken to improve the execution of the control?

Why it is important

Control activities should be part of the normal day-to-day activities of officials, as the routine will ensure consistency in application and effective implementation of controls.

If officials understand the importance of controls and how these further the objectives of the institution, they will be more disciplined in their execution and alert to areas where controls can be improved or are being circumvented.

If officials know they are safe to raise concerns about controls being circumvented and are actively encouraged to do so, accountability failures can be identified early in the process and dealt with.

Applicable legislation

Section 45(a) of the PFMA prescribes that an official in a department, trading entity or constitutional institution must ensure that the system of financial management and internal control established for that department, trading entity or constitutional institution is carried out within the area of responsibility of that official.

Section 57(a) of the PFMA stipulates that an official in a public entity must ensure that the system of financial management and internal control established for that public entity is carried out within the area of responsibility of that official.

Section 78(1)(a) of the MFMA states that each senior manager of a municipality and each official of a municipality exercising financial management responsibilities must take all reasonable steps within their respective areas of responsibility to ensure that the system of financial management and internal control established for the municipality is carried out diligently.

Controls accounting officers and authorities should implement

Accountability means that those performing actions or making decisions are answerable for them, but also that there should be consequences for transgressions, a lack of action and poor performance. Consequences should be instituted against officials who fail to comply with applicable legislation, continuously underperform or are negligent, as well as against those whose actions and decisions cause financial losses.

Officials should be clear on their responsibilities and the performance expected from them as well as on the consequences for transgressions and poor performance. Leadership should consistently but fairly implement the policies and procedures of the institution relating to consequences.

Questions oversight structures and executive authorities could ask to obtain assurance

1. How is it ensured that officials are aware of the consequences for poor performance and transgressions?
2. What is the standard process followed to enable consequence management if the following matters are identified:
   a. Irregular expenditure?
   b. Fruitless and wasteful expenditure?
   c. Unauthorised expenditure?
   d. Financial misconduct?
   e. Audit findings that point toward negligence and/or controls that failed?
   f. Possible fraud and the abuse of the supply chain management system?
   g. Transgressions of the institution's policies?
3. If findings on consequence management were raised by the external auditors (AGSA) and/or unauthorised, irregular or fruitless and wasteful expenditure has not been dealt with timeously:
   a. What failed in the process of dealing with these matters?
   b. What actions are being taken to improve the process?
4. Provide reports on investigations into allegations of fraud and financial misconduct and the progress and outcomes of the investigations.

Why it is important

When officials are not held accountable for their actions, the perception is created that such behaviour and its results are acceptable and tolerated. This could make even those that are giving their best under trying circumstances feel hopeless.

Applicable legislation

Section 38(1)(h) of the PFMA requires the accounting officer for a department, trading entity or constitutional institution to take effective and appropriate disciplinary steps against any official in the service of the department, trading entity or constitutional institution who contravenes or fails to comply with a provision of the act; commits an act which undermines the financial management and internal control system of the department, trading entity or constitutional institution; or makes or permits any unauthorised, irregular or fruitless and wasteful expenditure.

Section 51(1)(e) of the PFMA prescribes that an accounting authority for a public entity must take effective and appropriate disciplinary steps against any employee of the public entity who contravenes or fails to comply with a provision of the act; commits an act which undermines the financial management and internal control system of the public entity; or makes or permits any irregular expenditure or fruitless and wasteful expenditure.

Section 32(2) of the MFMA stipulates that a municipality must recover unauthorised, irregular or fruitless and wasteful expenditure from the person liable for that expenditure, unless the expenditure (a) in the case of unauthorised expenditure, is authorised in an adjustments budget; or certified by the municipal council, after investigation by a council committee, as irrecoverable and written off by the council; and (b) in the case of irregular or fruitless and wasteful expenditure, after investigating by a council committee, is certified by the council as irrecoverable and written off by the council.

Section 62(1)(e) of the MFMA states that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that disciplinary or, when appropriate, criminal proceedings are instituted against any official of the municipality who has allegedly committed an act of financial misconduct or an offence in terms of chapter 15 of the act.

What this guide is about

Preventative controls are measures built into the processes of an institution at transactional level to prevent errors, fraud or any failure to achieve specific objectives.

A preventative control can be in place, but for it to work effectively (in other words, in the right way, at the right time, every time) it must be built on a strong control environment.

The control environment is the set of standards, processes and structures that provides a basis for carrying out internal control across the institution.

A key element of this control environment is the institutionalised internal controls.

These are the controls that should be in place at an organisational level to enable the implementation and monitoring of, and assurance on, preventative controls.

This guide deals with the institutionalised internal controls that should be in place at institutions as the foundation for preventative controls.

Oversight structures and executive authorities can use this guide to require assurance from accounting officers and authorities (AO/AA) that these controls have been implemented and are working effectively – this is presented as questions to ask the AO/AA.

Implement suitable risk management

03

Controls accounting officers and authorities should implement

Appropriate risk management activities should be implemented 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.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Is there a documented integrated management strategy and risk assessment plan in place that considers the objectives of the institution and all the risks that potentially have an impact on the achievement of those objectives?
2. Does the risk identification process consider changes to external factors that can significantly affect the institution's ability to achieve its objectives?
3. How often is an assessment performed to identify emerging risks to the institution?
4. Does the risk assessment cover all critical financial management areas (e.g. supply chain management, financial sustainability, financial statement preparation, and asset management)?
5. Is the risk assessment used to identify deficiencies in internal control, which are then responded to in a timely manner?
6. What are the main financial management risks faced by the institution? What mitigations have been identified and what is the progress in implementing these mitigations?

Why it is important

Every institution faces a variety of risks from external and internal sources. Risks can be defined as the possibility that an event will occur and adversely affect the achievement of the institution's objectives.

Risk assessment forms the basis for determining how the risks will be managed. Risk assessment also requires management to consider the impact of possible changes in the external environment that may render internal control ineffective.

Knowing the risks and changes faced by an institution, and responding to the risks proactively through implementing appropriate controls, reduce the likelihood of failures in financial management and the non-achievement of objectives.

Applicable legislation

Section 38(1)(a)(i) of the Public Finance Management Act (PFMA) states that the accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 51(1)(a)(i) of the PFMA requires an accounting authority of a public entity to ensure that the public entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 62(1)(c)(i) of the Municipal Finance Management Act (MFMA) stipulates that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Controls accounting officers and authorities should implement

Policies and procedures should be established and communicated to enable and support the understanding and execution of internal control objectives, processes and responsibilities. The policies should cover all the main areas of decisionmaking, governance and control of the institution.

Standard operating procedures should be in place that specify the actions (including control activities) that should be taken to give effect to policies. The responsibility for executing the policies should be specified and clear.

The policies and procedures should be reviewed periodically to determine their continued relevance and should be updated when necessary.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Provide a register of all the policies of the institution. Based on the content of the register, questions can be asked to assess the completeness of the policies.

   The standard policies that should be in place are often defined in legislation; but in general, the main financial management policies should deal with the following:
   - Revenue (e.g. billing and taxes)
   - Supply chain management
   - Making payments
   - Asset management
   - Remuneration of employees
   - Subsistence and travel

03

Questions oversight structures and executive authorities could ask to obtain assurance (continued)

- Overtime
- Allowances (including acting allowances)
- Investments
- Debt collection

Questions can also be asked about the typical human resources-related policies, such as:

- Recruitment
- Performance management
- Disciplinary processes

2. Are there any long-outstanding draft policies that have not been approved by leadership?
3. How often should the policies of the institution be reviewed? Are these timelines adhered to?
4. Are documented standard operating procedures in place for all financial management processes of the institution?
5. If it was found (by the external auditors (AGSA), internal audit unit or another institution) that there are significant control deficiencies in a process of the institution:
   a. Did a policy of the institution provide the requirements for dealing with the specific matter? If a policy was in place, why was it not adhered to?
   b. Was a documented standard operating procedure in place that defines and describes the required control activities and who is responsible for them? If a procedure was in place, why was it not adhered to?
   c. What actions are being taken to improve the process?

Why it is important

The implementation of controls can only be successful if the control activities are defined, communicated and built into an official's day-to-day activities.

Policies and procedures are the vehicle for management to communicate their expectations of control and to hold officials accountable for implementation.

Applicable legislation

Section 38(1)(a)(i) of the PFMA prescribes that the accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 51(1)(a)(i) of the PFMA states that an accounting authority of a public entity must ensure that the public entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 62(1)(c)(i) of the MFMA stipulates that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Controls accounting officers and authorities should implement

An institution that demonstrates a commitment to competence should ensure that they attract and retain competent officials and invest in their continuous upskilling. Effective human resource management should be implemented to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored.

Job descriptions that detail expectations in terms of knowledge, skills, expertise and credentials needed to effectively carry out responsibilities should exist for each position (e.g. detailed job descriptions for financial reporting, performance reporting and compliance reporting positions).

The skills and competencies of officials should be evaluated regularly to establish whether they are still relevant and adequate to carry out the institution's objectives.

The institution should provide training to officials aimed at improving and maintaining the core skills and competencies required. Performance agreements should be in place to define the responsibilities of officials and what they will be held accountable for.

Officials' performance should be regularly monitored and evaluated based on signed performance agreements to identify areas of improvement and areas where officials are performing well.

The institution should have a process in place to reward and retain officials who are performing well.

Management should identify situations where the skills and experience of outsourced service providers (consultants) are required to assist in achieving the institution's objectives. Controls should be put in place to monitor the performance of consultants and to ensure that skills are transferred to the officials in the division where outsourced services are utilised.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Is a human resource plan in place that addresses the skills and qualifications required from all levels of officials, retention (succession planning), development of officials' skills (training), etc.?
2. Are vacancies and stability monitored for key officials? Are vacancies, capacity and resourcing monitored in key divisions?
3. Which key positions are currently vacant? How long have they been vacant and what steps are being taken to fill the positions?
4. Is there a strategy/policy in place to regulate the appointment and monitoring of consultants?
5. Are consultants contracted for functions where officials are also employed to perform the same function? Why was a consultant deemed necessary and how is it being ensured that skills are transferred?
6. What has the staff turnover been in the past year for the institution, senior management and specific divisions (e.g. finance)? What is the reason for the high/low turnover?

Why it is important

The effectiveness of control activities is dependent on skilled and experienced officials. Controls can also be automated but a skilled individual will still be required to manage the information technology controls or monitor the reports from the system to identify and respond to anomalies and errors.

Vacancies and prolonged acting periods create risks in the form of inadequate segregation of duties and a short-term approach toward implementing control.

03

Applicable legislation

The Public Service Act and Chapter 4 of the Public Service Regulations prescribe how employment matters should be dealt with at departments.

Chapter 7, part 4 of the Municipal Systems Act prescribes the requirements for staff matters at municipalities.

Controls accounting officers and authorities should implement

Independent assurance providers are those that independently look at the status of internal control and risk in order to provide an objective assessment to senior management and the AO/AA. The external auditors (AGSA) are independent assurance providers, but the internal audit unit and the audit committee are well placed internally to provide the required assurance.

There should be an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and recommends corrective action effectively.

The audit committee should promote 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.

Management should address the findings and recommendations from the internal audit unit and the audit committee. They should also develop and monitor the implementation of action plans to address any internal control deficiencies identified.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Has an internal audit unit been established?
2. Does the internal audit unit have enough competent, experienced and independent staff to conduct separate evaluations of the institution's internal control?
3. Does the internal audit unit communicate information about the strengths and deficiencies in internal control and make recommendations for improving internal control promptly to enable management to take corrective action?
4. Does management implement the internal audit recommendations?
5. Is an audit committee in place? What is the role of the audit committee?
6. How do the AO/AA make use of the expertise, advice and recommendations of the audit committee?
7. If it was found that the financial statements or performance report of the institution was not credible or that the institution materially did not comply with legislation:
    a. Were these deficiencies also identified by the internal audit unit and/or the audit committee?
    b. If it was identified, why was it not addressed?
    c. If not identified, why not?
8. Provide the latest report of the audit committee and the internal audit reports for the past year. How are the matters highlighted in these reports being addressed?

Why it is important

The AO/AA receive assurance from the senior management of the institution that controls are in place and that risks are managed. Senior management performs a supervisory or review function but in most part also relies on the assurance they receive from their subordinates that all is well.

Independent assurance providers provide an objective view of the status of internal control. The audit committee along with a strong internal audit unit is best placed to do so, as a result of their independence to identify and promptly act in situations where management overrides controls or deviates from expected standards of conduct.

Applicable legislation

Section 38(1)(a)(ii) of the PFMA states that the accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains a system of internal audit under the control and direction of an audit committee complying with and operating in accordance with regulations and instructions prescribed in terms of sections 76 and 77.

Section 51(1)(a)(ii) of the PFMA prescribes that an accounting authority for a public entity must ensure that the public entity has and maintains a system of internal audit under the control and direction of an audit committee complying with and operating in accordance with the regulations and instructions prescribed in terms of sections 76 and 77.

Section 62(1)(c)(ii) of the MFMA states that the accounting officer of a municipality is responsible for managing the financial administration of the municipality and must for this purpose take all reasonable steps to ensure that the municipality has and maintains effective, efficient and transparent systems of internal audit operating in accordance with any prescribed norms and standards.

Section 166(1) of the MFMA requires each municipality and each municipal entity to have an audit committee.

AUDITOR-GENERAL
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PREVENTATIVE
CONTROL GUIDE

GUIDE 04

PROCUREMENT OF GOODS AND SERVICES

What this guide is about

The importance of public procurement is illustrated by the fact that it has been afforded Constitutional status.

Section 217 of our country's constitution requires public sector institutions to contract for goods and services in accordance with a system that is fair, equitable, transparent, competitive and cost-effective. To give effect to this requirement, legislation is in place to regulate public procurement, including the Public Finance Management Act (PFMA) and the Municipal Finance Management Act (MFMA) together with their regulations.

Many public sector institutions are not complying with procurement legislation, as evidenced by the prevalence of irregular expenditure across all spheres of government and the AGSA's findings on procurement. Poor decisions in managing procurement, the abuse of systems and fraud lead to significant financial losses and the inability to deliver on government programmes, thereby affecting our country's citizens directly.

The process of inviting competitive bids, evaluating the bids received and awarding the contracts is well described in legislation and the guidance issued by the National Treasury.

Institutions generally have supply chain management (SCM) policies and procedures in place and have the required delegation frameworks, structures and committees to enable a controlled process. However, weaknesses arise when the standard procurement process is not followed or deviations are allowed.

This guide deals with the key preventative controls that should be in place at public sector institutions to reduce risks in the procurement of goods and services.

Oversight structures and executive authorities can use this guide to require assurance from accounting officers and authorities (AO/AA) that these preventative controls have been implemented and are working effectively – this is presented as questions to ask the AO/AA.

Use procurement plans to enable proper planning

04

Controls accounting officers and authorities should implement

Institutions must have an annual procurement plan, approved by the AO/AA, which includes detail on all the procurement requiring a competitive bidding process in that year and the timing thereof. Procurement should take place in accordance with the plan and any amendments should be approved by the AO/AA.

Departments and public entities submit the plans to the relevant treasury by 31 March of each year and progress against the plans is reported on a quarterly basis. Provincial treasuries can also request the plans of municipalities and municipal entities.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Was a procurement plan developed annually?
2. Did the AO/AA approve the plan and any amendments thereto?
3. How is the plan monitored – who is responsible for monitoring and how are deviations from the plan dealt with?
4. Does procurement take place in accordance with the plan? If not, what actions are being taken to address any non-adherence?
5. If it was found that the institution did not follow a competitive bidding process for contracts (i.e. there were deviations), contracts were extended, variations were done, or projects were delayed or not delivered as a result of poor procurement processes:
    a. Was the procurement included in the procurement plan?
    b. Why did the procurement not take place in accordance with the plan?

Why it is important

Proper planning reduces delivery delays, eradicates recurring contracts and unnecessary extensions, and eliminates the need for emergency procurement. Poor demand and procurement planning results in the inadequate development of specifications, wrong decisions about the items to be procured, and unrealistic cost estimates.

Applicable legislation

Section 38(1)(a)(i) of the PFMA states that the accounting officer for a department, trading entity or constitutional institution must ensure that that department, trading entity or constitutional institution has and maintains effective, efficient and transparent systems of financial and risk management and internal control. Section 51(1)(a)(i) of the PFMA prescribes similar requirements for an accounting authority of a public entity.

SCM Instruction Note 2 of 2016/17 issued by the National Treasury makes it mandatory for departments and public entities to plan for their procurement.

MFMA Circular No. 62 dated 20 August 2012 provides guidelines on the implementation of demand management and the submission of procurement plans at local government level.

Learn more about this control here

National Treasury website:

- SCM Instruction Note 2 of 2016/17: Procurement plans – submission and reporting
- MFMA Circular No. 62 dated 20 August 2012: Supply chain management: Enhancing compliance and accountability
- SCM Circular dated 29 July 2011: Guidelines on the implementation of demand management

In addition, the following are published:

- Procurement plans are published as bid opportunities at the beginning of each financial year
- Quarterly performance against procurement plans are published
- Quarterly reports on deviations from competitive bidding and extensions of contracts beyond prescribed thresholds are published

Ensure adequate capacity and skills for supply chain management

04

Controls accounting officers and authorities should implement

Institutions should have adequate capacity and the required skills in place. This means that:

- The tasks, roles and resources required for the SCM function have been defined and the institution's establishment is reflective of the capacity required.
- The positions of key officials (e.g. the head of the SCM unit) are filled and there is a low vacancy rate in the SCM unit.
- The competence and skills requirements for SCM officials are defined and recruitment is done in accordance with these requirements. Any competency gaps are identified and addressed through training and/or other development processes.
- The required competence and skills of those officials not in the SCM unit but involved in SCM processes (e.g. members of bid committees) are also clearly defined and any gaps addressed.
- SCM officials and all other officials involved in SCM processes are informed of, and trained on, the latest developments in SCM, including all legislation, instructions, practice notes and guidance from the National Treasury as well as any other reforms.

Questions oversight structures and executive authorities could ask to obtain assurance

1. How was the number and type of resources determined for the SCM unit? Are these sufficient?
2. Is the position of the head of the SCM unit filled? What is the vacancy rate in the SCM unit? What actions are being taken to address vacancies?
3. Were the required competence and skills of every position in the SCM unit defined, and on what were these based? What gaps have been identified and how are these being addressed?
4. Were the required competence and skills of non-SCM officials involved in SCM processes determined? What are the requirements for officials involved in the bid specification, evaluation and adjudication committees? What are the requirements for officials in the different units responsible for procuring goods and services through a quotation process?

Questions oversight structures and executive authorities could ask to obtain assurance (continued)

5. Is there a specific training curriculum to ensure that officials understand and can apply the SCM policy and processes?
6. How is the training kept up to date with latest developments?
7. How is it ensured that all new SCM developments and reforms are communicated within the institution and that those responsible for implementation have been trained?
8. If there were recent changes in SCM legislation or new reforms, processes or controls from the National Treasury or provincial treasuries, questions can be asked specifically on how these were disseminated and implemented at the institution.

Why it is important

Adequate capacity and skills ensure that the right decisions are made; correct processes are followed; and sufficient segregation of duties, supervision, review and monitoring are built into the procurement process.

Officials often claim ignorance of legislative requirements or reforms that need to be implemented – continuous updates and training are therefore required for officials to keep up to date with such changes.

Applicable legislation

Treasury regulation 16A.5.1 (applicable to departments, constitutional institutions and schedule 3A and 3C public entities) states that the AO/AA must ensure that officials implementing the institution's SCM system are trained and deployed in accordance with the requirements of the Framework for Minimum Training and Development issued by the National Treasury.

Section 119(1) of the MFMA states that the accounting officer and all other officials of a municipality or municipal entity involved in the implementation of the SCM policy of the municipality or municipal entity must meet the prescribed competency levels.

Municipal supply chain management regulation 8 further states that the training of officials involved in implementing an SCM policy should be in accordance with any treasury guidelines on SCM training.

Learn more about this control here

National Treasury website:

- Supply chain management: A guide for accounting officers of municipalities and municipal entities
- Chapter 6 of the Municipal Regulations On Minimum Competency Levels
- Public service regulation 74: Institutional arrangements regarding education, training and development
- Practice Note Number SCM 5 of 2004: Training of the supply chain management officials
- Practice Note Number SCM 4 of 2003: Code of conduct for supply chain management practitioners
- MFMA Circular No. 47 dated 13 February 2009: Capacity building and training

Controls accounting officers and authorities should implement

The institution should have well-established, effective and standardised processes for the procurement of goods and services. Officials should understand how procurement must be done and should be enabled to execute their duties in a consistent and effective manner.

The starting point is always an SCM policy that is comprehensive enough to cover all the typical procurement done by the institution but also deals with non-routine matters such as emergency procurement. The policy should be reviewed and updated regularly to ensure that it remains relevant and covers new risks identified.

Documented standard operating procedures for all types of procurement in line with the policy are required, with specific responsibilities to enable officials to understand what they are responsible for, including their responsibility for controls and how to perform their functions.

Automating procurement processes is an effective and proven way of ensuring a consistent and thorough approach in line with the operating procedures. Where automation is not possible, checklists should be developed and applied from the start of the process until the contract is awarded, and should be kept as an audit trail.

Standard templates, registers and filing/recording methods also assist officials to work in a fast, efficient and consistent manner.

Technical support should be available to officials if they are unsure or come across complex issues. Reaching out to the treasuries for support before a decision is made is more effective then seeking their support after a poor decision has already been made.

Questions oversight structures and executive authorities could ask to obtain assurance

1. When last was the SCM policy reviewed and updated?
2. Does the policy cover all types of procurement and areas of risk, including emergency procurement, using a sole supplier, deviations from the procurement process, unsolicited bids, extensions, and variations on contracts?
3. Are there documented standard operating procedures for all types of procurement in line with the policy?
4. Are the responsibilities of officials involved in the procurement process documented, including the controls for which they are responsible? Do they understand what they are responsible for and how to perform their functions? What specific measures are taken to ensure their level of understanding?
5. What tools (e.g. automation, checklists and templates) have been implemented at the institution to enable a consistent and thorough procurement process that reduces the risk of human error?
6. What technical support is available to officials if they are unsure or come across complex issues?
7. If it was found that there were failures in the procurement process of the institution resulting in irregular expenditure:
    a. What do the policy and procedures prescribe on this matter?
    b. Why did the standard procurement process and controls fail?
    c. What actions are being taken to improve the controls?
8. The chair of the audit committee and the head of the internal audit unit can be requested to share their reports and assessments on the effectiveness and standardisation of the procurement processes of the institution.

04

Why it is important

The SCM unit, members of committees and officials delegated to make decisions have a multitude of matters to consider and check.

The processes can be quite complex and lengthy, lending itself to human error and the risk of manipulation. Well-established, effective and standardised processes for the procurement of goods and services are therefore necessary.

Applicable legislation

Section 38(1)(a)(iii) of the PFMA states that the accounting officer for a department, trading entity or constitutional institution must ensure that it has and maintains an appropriate procurement and provisioning system that is fair, equitable, transparent, competitive and cost-effective. Section 51(1)(a)(iii) of the PFMA prescribes similar requirements for the accounting authority of a public entity.

Section 112(1) of the MFMA states that the SCM policy of a municipality or municipal entity must be fair, equitable, transparent, competitive and cost-effective, and comply with the prescribed regulatory framework for municipal SCM.

Learn more about this control here

National Treasury website:

- Supply chain management: A guide for accounting officers of municipalities and municipal entities
- MFMA Circular No. 62 dated 20 August 2012: Supply chain management: Enhancing compliance and accountability
- National Treasury instruction note on enhancing compliance monitoring and improving transparency and accountability in supply chain management

Controls accounting officers and authorities should implement

Even good procurement processes can fail as a result of undue influence in the process or officials not acting in good faith as they have a personal or financial interest in the process.

To safeguard the procurement process against conflicts of interest, the institution should:

- Define clearly (in a policy) what a conflict of interest entails in accordance with the applicable legislation, and ensure awareness and understanding of this across the institution.
- Design and implement processes whereby all officials annually declare their business interests and update the declaration throughout the year as circumstances change. Any official who did not complete such declarations should be identified and charged with misconduct.
- Have a process in place to test whether officials declared all of their interests – this can be done for specific officials with significant influence in the procurement process and on a sample basis for other officials.
- Ensure that business and personal interests of officials that could potentially create a conflict of interest are identified from the declarations made and the required safeguards are put in place to prevent them from having any influence on such a procurement process.
- Require all officials and persons from outside the institution (e.g. experts) who are part of a procurement process to declare whether they might have potential conflicts of interest. This should be standard practice at the meetings of bid specification, evaluation and adjudication committees as well as meetings of the accounting authority (e.g. board of directors) where procurement decisions are made.

Controls accounting officers and authorities should implement (continued)

- Include independent persons in the evaluation and adjudication committees for high-value procurement to reduce the risk of undue influence or pressure on members to favour certain suppliers. These include risk officers, internal auditors, treasury officials or experts from outside the institution.
- Require all suppliers to declare whether any state official, political office-bearer or any person involved in the procurement process has an interest in the supplier (business or personal) as a prerequisite for accepting their bid.
- Implement standard tests whereby possible conflicts of interest are identified for specific suppliers. This includes checking available information from treasuries on persons employed in the state and publically available databases such as that of the Companies and Intellectual Property Commission.
- Implement mechanisms for officials, suppliers and other role players to report any undue influence, fraud, unfair processes or other abuses of the system. The mechanisms must be strong in the areas of investigating all complaints/allegations and implementing remedial action.

Questions oversight structures and executive authorities could ask to obtain assurance

1. What percentage of officials of the institution completed their annual declaration of interest? What steps are being taken to address the out standing declarations?
2. What process is followed to verify whether officials declared all of their interests? What have been the general findings from the verification process?
3. Were any business or personal interests identified that could potentially create a conflict of interest? What safeguards were put in place to prevent officials with such interests from having any influence on a related procurement process?
4. Is the declaration of conflicts of interest in procurement processes a standard practice? How has it been implemented and has it proven to be successful?

Questions oversight structures and executive authorities could ask to obtain assurance (continued)

5. Explain the membership of the bid specification, evaluation and adjudication committees as defined in the SCM policy as well as the terms of reference of the committees. How are the members safeguarded from undue influence or pressure to favour certain suppliers, or prevented from doing so themselves?
6. Are prospective suppliers required to declare whether any state official, political office-bearer or any person involved in the procurement process has an interest in the supplier (business or personal) as a prerequisite for accepting their bid? How is 100% compliance to this requirement ensured?
7. What actions are taken to check whether suppliers declared all interests; in other words, how is the validity of their declarations verified?
8. What mechanisms are in place for officials, suppliers and other role players to report any undue influence, fraud, unfair processes or other abuses of the system? Provide reports on the number of allegations/complaints reported, the steps taken to investigate and deal with them, and the timelines involved. Where it was found that the complaint was valid, what was done to remedy the matter?
9. If it was found that there were unfair or uncompetitive procurement processes at the institution as a result of conflicts of interest:
    a. Which preventative control failed?
    b. What actions are being taken to improve the control?

Why it is important

Undue influence in the procurement process and the favouring of certain suppliers to the exclusion of others increase the risk of suppliers being awarded contracts on which they then cannot deliver and institutions paying too much for goods and services, resulting in value for money not being obtained and projects failing. The procurement process should therefore be safeguarded against conflicts of interest to prevent fraud and the abuse of the SCM system.

Applicable legislation

Section 50(1)(b) of the PFMA (applicable to schedule 2, 3B and 3D public entities) states that an accounting authority must act with fidelity, honesty, integrity and in the best interest of the public entity in managing the financial affairs of the public entity.

Treasury regulation 16A.8.1 (applicable to departments, constitutional institutions and schedule 3A and 3C public entities) states that all officials and other role players in an SCM system must comply with the highest ethical standards. Treasury regulation 16A.8.3(a) further states that an SCM official or other role player must recognise and disclose any conflict of interest that may arise.

Section 117 of the MFMA explicitly states that councillors are prohibited from serving on municipal tender committees, while section 118 of the MFMA further prohibits interference with the SCM system, including amending or tampering with any tender, quotation, contract or bid after submission.

Section 112(1)(j) of the MFMA requires the compulsory disclosure of any conflicts of interest that prospective contractors may have in specific tenders and the exclusion of such prospective contractors from those tenders.

Learn more about this control here

National Treasury website:
- General procurement guidelines
- Supply chain management: A guide for accounting officers of municipalities and municipal entities
- Practice Note Number SCM 4 of 2003: Code of conduct for supply chain management practitioners
- Practice Note Number 7 of 2009/2010: Supply chain management: Declaration of interest: Amendment and augmentation of standard bidding document (SBD 4)
- MFMA Circular No. 62 dated 20 August 2012: Supply chain management: Enhancing compliance and accountability
- National Treasury instruction note on enhancing compliance monitoring and improving transparency and accountability in supply chain management

AUDITOR-GENERAL
SOUTH AFRICA

PREVENTATIVE
CONTROL GUIDE

GUIDE 05

PREPARATION OF FINANCIAL STATEMENTS

PREPARATION OF FINANCIAL STATEMENTS

GUIDE 05

What this guide is about

The purpose of the financial statements is to present a true and fair view that is useful to a wide range of users of an institution's financial performance, financial position, changes in net assets and cash flows.

Financial statements also show the results of the stewardship and accountability of management for the resources entrusted to them.

Legislation therefore requires public institutions to keep full and proper records of the financial affairs of the institutions and prepare financial statements in accordance with the accounting framework prescribed for that type of institution.

Information contained in the financial statements shows, amongst other matters, how the institution spends the money entrusted to it by the public, how much it owes creditors, how much is owed to the institution, and whether it is expected that the money owed will be received. The financial statements also provide crucial information on how the budget was adhered to, the unauthorised, irregular as well as fruitless and wasteful expenditure incurred plus the overall financial position of the institution, reflecting whether its operations are financially sustainable.

The financial statements are used by the committees in Parliament, legislatures and councils to call the heads of institutions to account and to make decisions on, for example, the allocation of the budget. In the case of some institutions, the financial statements are also used by creditors, banks and rating agencies to determine the level of risk in lending money to an institution.

Many public sector institutions do not manage to prepare credible and quality financial statements in line with the legislative requirements and the applicable accounting framework, and to submit these in time for auditing. Submitted financial statements are often also not supported by complete and accurate records and reliable documentation.

Controls to prevent misstatements are inadequate and the misstatements remain undetected even though the financial statements go through various levels of review. Too much reliance is placed on the annual external audit process to identify misstatements in the financial statements and report them for correction.

This guide deals with the key preventative controls that should be in place at public sector institutions to ensure quality and credible financial reporting. Oversight structures and executive authorities can use this guide to require assurance from accounting officers and authorities (AO/AA) that these preventative controls have been implemented and are working effectively – this is presented as questions to ask the AO/AA.

Controls accounting officers and authorities should implement

Institutions should have adequate capacity and the required skills in place. This means:

- The tasks, roles and resources required for the accounting and reporting function have been defined and the institution's establishment is reflective of the capacity required.
- The positions of key officials (including the chief financial officer and financial managers) are filled, stability is maintained in these positions, and there is a low vacancy rate in the rest of the finance unit.
- The qualifications, competence and skills requirements for finance officials are defined and recruitment is done in accordance with these requirements
  Any competency gaps are identified and addressed through training and/or other development processes.
- Regular training is provided to those responsible for accounting and reporting to enable them to correctly interpret and apply current and updated accounting standards.

Where complex accounting matters arise and the institution does not have the current capacity to attend to these matters appropriately, suitably skilled consultants can be brought in to assist. The agreement with the consultants should ensure the transfer of the required skills for the institution to be able to handle the matters in-house in future. The institution should also monitor the consultants to ensure that they deliver on their commitments as agreed.

Questions oversight structures and executive authorities could ask to obtain assurance

1. How were the skills and the staff complement required in the finance unit determined by the institution? Are these sufficient?
2. Is the position of chief financial officer filled? What is the vacancy rate in the finance unit? What actions are being taken to address vacancies?
3. Were the required competence and skills of every position in the finance unit defined, and on what were these based? What gaps have been identified and how are they being addressed?
4. Is there an annual training plan for ensuring that officials are kept up to date with amendments to the accounting frameworks?
5. Were consultants brought in to assist with some areas of reporting? Which areas were these and how was it ensured that skills were transferred to officials of the institution during this process?
6. What processes were implemented to ensure that the consultants delivered on their commitments as agreed? Was it concluded from these processes that the consultants delivered as required?
7. If the institution received audit findings in relation to not complying with specific requirements of, or amendments to, the financial reporting framework, the institution may be requested to indicate how it has been ensured that its officials now understand how to apply the specific requirements or amendments to avoid misstatements in these areas going forward.
8. Audit committees provide independent assurance over the financial reporting processes. The observations of the chair of the audit committee on the capacity of the finance unit may be requested.

Why it is important

The institution needs sufficient capacity to be able to independently prepare financial statements that are compliant with the prescribed accounting framework and applicable legal requirements. It is for this reason that the preparers of the financial records have to be well versed in the principles as prescribed by the financial reporting framework relevant to their institution and applicable legal requirements, including tax implications. They have to attend regular training on any updates to the financial reporting framework and legislation to ensure that their knowledge and skills remain sufficient.

Stability in key finance positions is required because different institutions enter into different types of transactions, based on the nature of the business. Institutional knowledge, which is gained over time, is required to understand and appropriately account for these transactions.

Applicable legislation

Section 83 of the Municipal Finance Management Act (MFMA) requires the accounting officer, senior managers, chief financial officer and other financial officials of a municipality to meet the prescribed financial management competency levels. A municipality must for this purpose provide resources or opportunities for the training of these officials to meet the prescribed competency levels.

Section 107 of the MFMA states that the accounting officer, senior managers, chief financial officer and all other financial officials of a municipal entity must meet the prescribed financial management competency levels.

Learn more about this control here

National Treasury website:

- Chief financial officers' handbook for departments
- Chief financial officers' handbook for municipalities

Implement standardised, effective accounting processes

05

Controls accounting officers and authorities should implement

The institution should have well-established, effective and standardised processes for daily and monthly accounting disciplines. Officials should understand what should be done and should be enabled to execute their duties in a consistent and effective manner. Documented standard operating procedures should be required for all types of transactions that the institution can enter into. These procedures should assign specific responsibilities to enable officials to understand what they are responsible for, including their responsibility for controls and how to perform their functions.

The documented procedures should address every action required from the point of initiation of a transaction through to accounting for the transaction in the general ledger of the institution. A separate process should also be documented and implemented for the compilation of the financial statements from the information recorded in the general ledger.

As an example, the process for revenue transactions should start from receipt of a request for service delivery. It should then address the delivery of the service, invoicing and creation of a debtor, following up on payment, receipt of payment either in cash or electronically, issuing of a receipt, and the daily banking and allocation of the receipt to the correct account. The processes should include clear segregation of duties between different officials to minimise the opportunity for an official to, for instance, receive cash and not record it.

Automated controls for the verification of the accuracy and completeness of transactions and accounting records should be built into the system of accounting to reduce the possibility of human error or omission.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Does the institution have documented standard operating procedures for all transaction types that it enters into?
2. Do supervisors explain these procedures to the officials responsible for carrying out the transactions before they commence any new functions? Are supervisors also readily available to provide support to officials when they encounter difficulty with any of the functions allocated to them?
3. If the institution has a large volume of transactions in any area, are automated systems used for the capturing of these transactions and do these automated systems have built-in quality checks? Are there any transaction and accounting processes that are not automated?
4. Are functions that could provide an opportunity for fraud, theft or undetected errors if they are allocated to the same individual, such as both the receipt and the recording of funds, segregated between different individuals?
5. How does the institution identify and respond to breaches of the standardised procedures?
6. If the institution received external audit findings about misstatements in the submitted financial statements, the following may be asked:
   a. Is the relevant matter addressed by the standard operating procedures and what do the procedures prescribe in this area?
   b. Why were the procedures not effective in preventing the misstatement?
   c. How have the procedures or their implementation been improved to prevent similar misstatements in future financial reports?
7. The internal audit unit is responsible for evaluating the effectiveness of the controls of the institution and should regularly report to management and the audit committee on these matters. The evaluation of whether standardised and effective processes are implemented at the institution falls within the scope of this responsibility. The audit committee provides oversight of the functions of the internal audit unit. The audit committee chair and chief audit executive may be requested to provide the internal audit reports produced from carrying out this function.

Why it is important

When officials are well aware of every step expected of them, incompatible functions are separated and the automated systems in which transactions are logged and recorded have built-in quality checks, it is much less likely that transactions will go unrecorded or be recorded inaccurately.

The ability to clearly identify – through these documented processes – which official is accountable for which steps also enables management to quickly and effectively implement consequence management and take corrective action where the process has not been followed as required.

Applicable legislation

Section 38(1) of the Public Finance Management Act (PFMA) states that the accounting officer for a department, trading entity or constitutional institution must ensure that that department, trading entity or constitutional institution has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 51(1) of the PFMA also requires an accounting authority for a public entity to ensure that that public entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Section 62(1) of the MFMA determines that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control.

Learn more about this control here

National Treasury website:

- Chief financial officers' handbook for departments
- Chief financial officers' handbook for municipalities

Controls accounting officers and authorities should implement

Proper record keeping means that transactions are processed in a complete, accurate and timely manner and that the availability of sound and up-to-date records is facilitated to support in-year and year-end financial reporting.

Documents used for processing transactions should be kept in an orderly filing or record management system to allow for easy retrieval during the performance of checks and reviews by those assigned the responsibility for monitoring the accounting and reporting activities.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Are the financial accounts of the institution up to date with all transactions that occurred in the past month? What is the status of suspense/reconciling accounts (in other words, accounts that include transactions that have not been allocated to their correct accounts yet)?
2. How are documents filed and safeguarded by the institution?
3. If the institution received audit findings in the past in respect of transactions not being completely recorded in the correct accounting period and/or financial statement items not being supported by reliable evidence, the following may be asked:
    a. How has the institution ensured that transactions in the identified area will in future be recorded completely and timeously?
    b. How did the institution improve its document management system to ensure that supporting documents will be readily available in future when the auditors request them?
4. The internal audit unit is responsible for evaluating the effectiveness of the controls of the institution and should regularly report to management and the audit committee on these matters. The evaluation of whether proper record keeping and document management is in place at the institution falls within the scope of this responsibility. The audit committee provides oversight of the functions of the internal audit unit. The audit committee chair and chief audit executive may be requested to provide the internal audit reports produced from carrying out this function.

Why it is important

To be useful in informing management's decisionmaking, financial management information needs to be up to date and reported in time.

A lack of financial discipline results in records being incomplete or inaccurate, due to accounting staff no longer having sufficient information on what had occurred in the past.

Documentation that is not filed in time may also be lost or misplaced, making it very difficult to retrieve the information when required.

Applicable legislation

Section 40(1) of the PFMA states that the accounting officer for a department, trading entity or constitutional institution must keep full and proper records of the financial affairs of the department, trading entity or constitutional institution in accordance with any prescribed norms and standards.

Section 55(1) of the PFMA also requires that the accounting authority for a public entity must keep full and proper records of the financial affairs of the public entity.

Section 62(1)(a) of the MFMA determines that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that full and proper records of the financial affairs of the municipality are kept in accordance with any prescribed norms and standards.

Learn more about this control here

National Treasury website:
- Chief financial officers' handbook for departments
- Chief financial officers' handbook for municipalities

Controls accounting officers and authorities should implement

Reviewers with the appropriate knowledge and skills as well as relevant qualifications should regularly review the accounting records. This should include performing spot checks of the records to the underlying documentation supporting the transactions.

The function of review and reconciliation should be segregated from the function of recording, which means that these functions should be assigned to different individuals in order for the review to be effective.

This is to ensure independent monitoring that transactions are recorded timeously, accurately and completely and to proactively identify and facilitate corrective action where accounting procedures are not being implemented as they should.

Registers should be kept for consumables, assets and liabilities such as inventory; property, plant and equipment; and capital commitments. It also needs to be ensured through reviews, counts and spot checks that these registers accurately and completely reflect the underlying assets and liabilities. These registers should be kept and maintained by individuals separate from the function of recording transactions in the accounting system.

Accounting staff should perform periodic in-year and year-end reconciliations between accounting records and the registers or statements that support these.

These reconciliations should be reviewed by senior accounting staff and any adjustments required from the reconciliations should be approved and made in line with the institution's delegated responsibilities.

More insights into the segregation of duties as they apply to property, plant and equipment are discussed in *Preventative control guide 6* dealing with asset management.

Questions oversight structures and executive authorities could ask to obtain assurance

1. How often are the accounting records reviewed and at which level is this done?
2. Are the functions of recording and review segregated at the institution?
3. What are the types of exceptions that have been identified from these reviews and how were these resolved?
4. Are registers of assets and liabilities kept and maintained by officials separate from recording in the accounting system?
5. What types of reconciliations take place at the institution and how often are these performed?
6. If an audit finding has been raised in the past in respect of accounting records not reconciling to underlying registers, what corrective measures have the institution implemented to prevent the same mistakes from happening in the future?
7. The internal audit unit is responsible for evaluating the effectiveness of the controls of the institution and should regularly report to management and the audit committee on these matters. The evaluation of whether review and reconciliation takes place at the institution falls within the scope of this responsibility. The audit committee provides oversight of the functions of the internal audit unit. The audit committee chair and chief audit executive may be requested to provide the internal audit reports produced from carrying out this function.

Why it is important

Independent review provides a mechanism for a senior staff member segregated from the recording function to check the records and identify any discrepancies that require investigation or resolution. This independent review is important as accounting staff may not recognise or want to admit to their own errors. Knowing that a review will be done increases the incentive to ensure that work is done accurately, completely and in accordance with the accounting policies of the institution.

The reconciliation of records to registers provides additional independent assurance on the reliability of the records when the records and registers are maintained by separate individuals.

Applicable legislation

In addition to the requirement for effective, efficient and transparent systems of financial and risk management and internal control prescribed by sections 38(1) and 51(1) of the PFMA as well as section 62(1) of the MFMA, treasury regulation 15.10.1.1(j) specifically requires reconciliations of the bank accounts of departments to be performed.

Learn more about this control here

National Treasury website:

- Chief financial officers' handbook for departments
- Chief financial officers' handbook for municipalities

Controls accounting officers and authorities should implement

The year-end financial statements that are submitted for auditing cannot be the first set of financial statements that the finance unit of the institution prepares for the financial year.

Senior accounting staff should also compile quality quarterly and half-yearly financial statements to facilitate the monitoring of financial reporting.

These reports should be reviewed by the chief financial officer within a reasonable time to obtain assurance that accounting officials are capacitated and enabled to produce credible financial statements and to identify any areas where the quality of the financial statements is not yet up to standard early on.

Controls can then be strengthened in these areas and support can be obtained in the form of training or assistance from consultants, where required, to ensure that the identified deficiencies are addressed before the year-end financial reporting.

Financial audit areas that had previously received a modified opinion should be identified and included in a corrective action plan. Focus should be placed on reviewing and ensuring the improvement of the quality of reporting in these areas.

These areas should be included in the risk assessment performed by the internal audit unit to inform their work plan; therefore, in-year reporting in these areas should be subjected to review by the internal auditors.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Does the institution produce interim financial statements? If yes:
   a. When and by whom are these reviewed?
   b. Have any concerns recently been identified from these reviews and how have these been addressed?
2. If external audit findings had previously been raised on the quality of the financial statements, how have these matters been addressed in the preparation of the interim financial statements?
3. Where external audit findings were raised on the quality of the financial statements and these areas were included in the internal audit unit's risk assessment and plan, the internal audit unit may be requested for their report on the implementation of in-year financial reporting and the effectiveness of corrective action implemented by the institution on prior year audit findings.

Why it is important

Regular reporting will strengthen the capacity of the finance unit to be able to produce credible financial reports within a specified time. Areas that previously included errors can be identified early on and the adequate correction of these can be tested by reviewing the information in the in-year reports well ahead of year-end financial reporting.

05

Applicable legislation

Treasury regulations 5.3.1, 29.3.1 and 30.2.1 require the AO/AA for national and provincial government institutions to establish procedures for quarterly reporting on the institution's performance. The performance of the institution includes financial performance and therefore interim financial reporting will be required as part of these procedures.

Sections 72 and 88 of the MFMA require municipalities and municipal entities to perform half-yearly assessments of the institution's performance, which includes financial performance and progress with resolving matters identified from the previous year's annual report.

Learn more about this control here

National Treasury website:
The National Treasury's annual instruction note on interim financial statements provides more information on the preparation and submission of interim financial statements by national and provincial departments for the financial periods ended 30 June, 30 September and 31 December.

Controls accounting officers and authorities should implement

The preparation of financial statements should commence as early as possible after the financial year-end of the institution to allow for a proper process of compilation, followed by several layers of review and correction of any findings from these reviews, well in time for submission to the external auditors (AGSA) by the legislated due date.

The financial statements should be prepared in accordance with the standardised accounting processes of the institution.

After preparation, the following layers of review should be performed on the financial statements:

- Review by the chief financial officer, followed by corrections from the review, followed by a re-review by the chief financial officer to ensure that all findings from the review have been appropriately addressed.
- Review by the audit committee, followed by corrections from the review, followed by a re-review by the audit committee to ensure that all findings from the review have been appropriately addressed.
- Review by the AO/AA, followed by corrections from the review, followed by a re-review by the AO/AA to ensure that all findings from the review have been appropriately addressed.

Financial audit areas that had previously received a qualified audit opinion should be identified and included in a corrective action plan. Focus should be placed on these areas during the review processes, to ensure improvement of the quality of reporting in these areas.

Questions oversight structures and executive authorities could ask to obtain assurance

1. When does the preparation of the financial statements commence?
2. When is the first draft set of financial statements submitted for review to the chief financial officer?
3. To which other layers of review are the financial statements subjected and how much time is provided for these review and correction processes?
4. When is the final draft set submitted to the AO/AA for review and approval?
5. How is it ensured that financial audit areas that received audit qualifications in the past are afforded more focused attention during the review processes?
6. The audit committee provides independent oversight during the external audit process and can be approached to comment on their evaluation of the implementation and effectiveness of the financial statements review processes before submission to the external auditors (AGSA).

Why it is important

It is important to provide sufficient time for reviewing the financial statements to ensure that any deficiencies in the quality thereof can be identified and corrected before the financial statements are submitted to the external auditors (AGSA).

Not providing sufficient time for review can result in the institution not being able to submit its financial statements for auditing by the legislated deadline, which will result in non-compliance with the applicable legislation for financial statements submission.

Applicable legislation

Sections 40(1)(b) and 55(1)(b) of the PFMA and section 122(1) of the MFMA make the AO/AA responsible for the preparation of financial statements that fairly present the state of affairs of the institution in accordance with the required accounting frameworks. Although the requirement for review is not specifically mentioned, the AO/AA would need to ensure that proper reviews are performed on these financial statements, including performing their own review in order to discharge this responsibility.

Learn more about this control here

National Treasury website:
- Chief financial officers' handbook for departments
- Chief financial officers' handbook for municipalities

In addition, the National Treasury publishes an annual instruction note on financial year-end procedures for national and provincial departments.

AUDITOR-GENERAL
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PREVENTATIVE
CONTROL GUIDE

GUIDE 06

ASSET MANAGEMENT

What this guide is about

The assets of a public sector institution form part of the resources it requires to pursue its service delivery and/or business objectives. The management of these assets includes deciding on which assets to use for which purpose and where and how to use the assets. It is therefore imperative that the management of the institution is well-informed and frequently updated on the assets that the institution holds and the current use and condition of these assets. This needs to inform the decisions related to acquisition, safeguarding, maintenance and disposal.

Legislation places the responsibility for the effective, efficient, economical and transparent use of the resources of the institution on the accounting officer. The accounting officer is also specifically tasked with the management, including the safeguarding and maintenance, of assets.

Non-adherence to these responsibilities is likely to result in losses or the incurrence of fruitless and wasteful expenditure due to theft, deteriorating assets or assets owned and paid for not being utilised.

Audit outcomes demonstrate that in many cases the controls over asset management are not effective. This typically results in the following deficiencies:

- Asset registers not being updated regularly.
- Asset registers not being reconciled to the accounting records resulting in material differences between the asset register and financial records.
- Assets that are under the control of the institution not being included in the asset register.
- Asset registers not containing sufficient detail to enable the identification of the physical assets recorded in these registers.

This guide on preventative controls in asset management focuses on the management of assets when these are already controlled by the institution. The guide addresses the category of assets referred to in the accounting frameworks as property, plant and equipment. Assets falling in this category include land and buildings, plant and machinery, vehicles as well as furniture and equipment.

This guide will assist with key preventative controls that need to be implemented by institutions in the management of assets to minimise the potential for errors in the recording of assets and potential losses to the institution. Oversight structures and executive authorities can use this guide to require assurance from accounting officers and authorities (AO/AA) that these preventative controls have been implemented and are working effectively – this is presented as questions to ask the AO/AA.

Controls accounting officers and authorities should implement

An institution must firstly identify all the assets under its control or ownership and where all these assets are. Ownership and/or control of assets should be supported by purchase documentation and contracts, or documents of title, which should be properly kept and easily retrievable by the institution for reviews and checks to be performed.

The identification of the assets will enable the institution to prepare a complete asset register of the assets under its control. All available sources should be used in determining the complete record of assets under the control of, or belonging to, the institution. These can include:

- Title deed searches for properties registered in the name of the institution
- Agreements for assets to be transferred from other structures of government
- Review of legislation determining custodianship of assets
- Registers and records currently kept by the institution in different locations
- Physical verification of assets at all identified premises of the institution

It should be ensured that all assets are easily identifiable by using barcodes, if possible, or descriptions of the exact location and details of the asset in the asset register.

Secondly, the institution must perform a conditional assessment of all its assets to determine the state of the assets. The conditional assessment of the assets will enable management to plan whether any assets should be disposed of or refurbished and when and how often maintenance should be performed.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Does the institution have a complete record of all the assets under its control?
2. Which completeness checks were performed by the institution to ensure that no assets owned or controlled by the institution were missed in compiling the record?
3. Does the record of assets indicate the location of each asset and provide a sufficient description or identification number to enable the identification of the physical asset?
4. Does the record of assets describe the condition of the asset in sufficient detail?
5. Internal audit units regularly perform audits on asset management as they are required by legislation to focus their efforts on key risks of the institution. The chief audit executive may be asked for his/her observations on the asset records of the institution. The chair of the audit committee may also be asked for the committee's observations as an independent assurance provider.

Why it is important

Service delivery and other objectives are likely to be compromised if an institution is unaware of which enabling assets belong to them.

Without a complete record of all the assets and their location, assets will be left unattended and unmaintained without any accountability being taken for them.

The identification of assets will, however, inform the institution which assets they have available to enable service delivery.

A lack of conditional assessments will result in assets not being adequately maintained. Conditional assessments are also essential to provide information on when assets should be decommissioned to avoid the risk of these assets becoming a hazard to the safety of citizens.

Applicable legislation

Section 38(1)(b) of the Public Finance Management Act (PFMA) states that the accounting officer for a department, trading entity or constitutional institution is responsible for the effective, efficient, economical and transparent use of the resources of the department, trading entity or constitutional institution. These resources include the institution's assets and a complete record of them to enable their management.

Section 6(1)(a) of the Municipal Finance Management Act (MFMA) determines that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the resources of the municipality are used effectively, efficiently and economically. Furthermore, section 63(2) of the MFMA requires the accounting officer to take all reasonable steps to ensure that the municipality has and maintains a management, accounting and information system that accounts for the assets and liabilities of the municipality; and that the municipality has and maintains a system of internal control of assets and liabilities, including an asset and liabilities register, as may be prescribed.

These requirements are also applicable to municipal entities as per sections 96(2)(a) and 96(2)(b) of the MFMA.

Learn more about this control here

National Treasury website:

- Guidelines issued in terms of the Asset Management Framework
- Local government capital asset management guideline

Controls accounting officers and authorities should implement

Controls to manage the access to, and custody of, assets should be implemented to prevent theft, unauthorised use, damage and the deterioration of assets. The custody controls should include procedures that specify how assets need to be stored, secured, treated and maintained.

The records of the assets in the custody of the institution need to be kept up to date to enable safeguarding and control over the appropriate use of these assets.

All new assets should be recorded in a register at the point of acquisition and physical counts should be performed on a regular basis to confirm and ensure that the register accurately and completely reflects the physical assets owned and controlled by the institution.

Based on the conditional assessments of assets, a maintenance plan specifying when and how often which assets will be maintained should be established. The maintenance plan should be used to inform the budget of the institution, to ensure that funds will be available for maintenance when required.

Maintenance is critical to ensure that capital assets continue to operate at optimal levels of effective, efficient and economical service delivery and to prevent assets from having to be replaced at great expense.

Questions oversight structures and executive authorities could ask to obtain assurance

1. How does the institution ensure that its assets are safeguarded against theft, misuse or damage?
2. Do the measures in place to safeguard assets cover all of the assets as per the institution's records?
3. How many cases of theft, loss or damage of assets have been recorded in the past financial year and what additional measures has the institution put in place to avoid future recurrences?
4. How often is maintenance on assets done? [This question can be asked in relation to the specific classes of assets that the institution has, e.g. how often is maintenance done on vehicles?]
5. Which assets have been identified that are obsolete? Were these assets at the end of their life cycle as per the asset strategy? If not, how did the assets become obsolete and what measures have been put in place to avoid assets becoming obsolete prematurely in future?
6. Internal audit units regularly perform audits on asset management as they are required by legislation to focus their efforts on key risks of the institution The chief audit executive may be asked for his/her observations on the safeguarding and maintenance of the institution's assets. The chair of the audit committee may also be asked for the committee's observations as an independent assurance provider.

06

Why it is important

As the assets of the institution form an integral part of the resources required to deliver services, these assets need to be protected and preserved to ensure their continued availability for use.

All new assets need to be recorded as soon as they come under the control of the institution to ensure that these can be safeguarded effectively and that any potential loss or deterioration can be prevented or managed. Keeping the asset records up to date will ensure that assets can continue to be safeguarded and maintained.

Controls to secure assets are required as certain types of assets such as laptop computers are at a high risk of being stolen. Assets such as infrastructure are again at risk of being damaged and/or vandalised and losing their potential to provide economic benefits. Security measures will need to be implemented to prevent damage to such assets.

Controls to prevent unauthorised use will deter the misuse or the inappropriate use of assets. A lack of controls will result in these assets deteriorating more rapidly and not being able to deliver at optimal levels.

The maintenance of assets is essential to ensure their continued effective operation throughout their lifetime. For example, infrastructure and vehicles that are not maintained will eventually cease to operate and require replacement at great cost to the public purse.

Applicable legislation

Section 38(1)(d) of the PFMA states that the accounting officer for a department, trading entity or constitutional institution is responsible for the management, including the safeguarding and the maintenance, of assets. Furthermore, treasury regulation 10.1.1(a) requires the accounting officer of an institution to take full responsibility and ensure that proper control systems exist for assets and that preventative mechanisms are in place to eliminate theft, losses, wastage and misuse.

Section 63(1)(a) of the MFMA determines that the accounting officer of a municipality is responsible for the management of the assets of the municipality, including the safeguarding and the maintenance of those assets.

Learn more about this control here

National Treasury website:

- Guidelines issued in terms of the Asset Management Framework
- Local government capital asset management guideline

Ensure segregation of duties in management of assets

06

Controls accounting officers and authorities should implement

Institutions should implement policies and procedures to govern the management of assets by the institution, and these should assign clear accountability and responsibilities to identified individuals.

The segregation of duties should be prescribed by these policies and procedures to ensure that the following functions are performed by independent individuals:

- Custody and recording of assets
- Review and reconciliation

Staff members assigned custodianship of assets should periodically physically inspect assets and ensure that the information on assets in their custody agrees to the number of assets and the descriptions of these in the asset register.

The accuracy and completeness of the asset register should be regularly and independently reviewed by the asset manager.

An independent record of assets should be kept in the accounting system by the finance unit based on the balances carried forward from the prior period and the processing of any acquisitions or disposals of assets within the current period.

A reconciliation should be performed periodically between the asset accounting records and the asset register and any differences should be resolved by investigating the reason for the difference and making the required adjustments, authorised in terms of the institution's delegation framework, to either the asset register or the accounting record.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Does the institution have approved and documented systems of delegation and accountability?
2. Are the following functions allocated to separate individuals as per this system:
   - Custody and recording of assets
   - Review and reconciliation
3. Has any collusion been identified between employees in the asset management system? If so, how was the specific cases addressed and how was the system strengthened to reduce the possibility of collusion occurring in future?
4. Are the accounting records reconciled back to the asset register on a regular basis?
5. Which exceptions have been identified from the performance of these reconciliations?
6. If exceptions have been identified, how have these been addressed by correcting the accounting records or asset register; and how have controls been strengthened to improve correlation between the accounting records and asset register?
7. If the assets disclosed in the financial statements were previously qualified because the values did not reconcile to the asset register, what corrective actions have been implemented to ensure that the qualification does not occur again in future?
8. Internal audit units regularly perform audits on asset management as they are required by legislation to focus their efforts on key risks of the institution The chief audit executive may be asked for his/her observations on the segregation of duties in the management of assets. The chair of the audit committee may also be asked for the committee's observations as an independent assurance provider.

Why it is important

The segregation of duties is an essential element of effective preventative controls as it reduces the risk of errors or illegal events occurring since it facilitates the checking or authorisation of one individual's actions by another.

It is also especially essential for the custody and recording of assets to be segregated. The reason for this is that if an individual has control of an asset and keeps the records pertaining to the asset, the record of the asset can be made to agree with the physical assets on hand and therefore an opportunity arises for the assets to be misappropriated.

Why it is important (continued)

This being said, the segregation of duties can only be effective if there is no opportunity for collusion by separate individuals – management will have to remain alert to any indications that collusion may be occurring.

The review and reconciliation of asset records to the underlying assets is required to be able to identify, investigate and resolve any differences and therefore ensure that the number and value of assets reported in the financial statements are reliable.

Applicable legislation

Compliance with the legislative requirements to have adequate controls for asset management per section 38(1)(b) of the PFMA and sections 6(1)(a), 63(2)(a) and (c) and 96(2)(a) and (b) of the MFMA will be enabled by ensuring that duties within the control system are segregated.

Furthermore, the segregation of duties will strengthen the institution's ability to comply with the legislative requirements to safeguard and maintain assets as per section 38(1)(a) of the PFMA, treasury regulation 10.1.1(a) and section 63(1)(a) of the MFMA.

Learn more about this control here

National Treasury website:

- Guidelines issued in terms of the Asset Management Framework
- Local government capital asset management guideline

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PREVENTATIVE
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GUIDE 07

INFRASTRUCTURE DELIVERY PROCESS

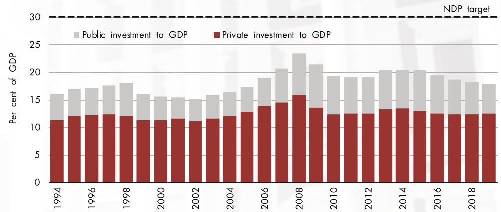
What this guide is about

The availability of appropriate infrastructure is crucial to service delivery in South Africa.

The proper development and management of infrastructure facilitates the implementation of key programmes in areas such as healthcare, education, human settlements, roads, and water and sanitation; and is vital for economic growth and employment. According to the 2020-21 public sector infrastructure expenditure and estimates, government invested approximately R226 billion in infrastructure in 2020-21.

The National Development Plan (NDP) targets capital investment of 30% of the gross domestic product (GDP) by 2030. Not only is the total investment by both the public and the private sector well below this target, it has also been continuously declining over the past few years. As a result, economic growth is slowed down and job creation is hampered.

Public and private sector capital investment as a share of GDP, 1994-2019



Source: National Treasury public sector infrastructure update

Spending on infrastructure forms a major part of government's budget at national, provincial and local government level.

Legislation places the responsibility for the effective, efficient, economical and transparent use of the resources of the institution on the accounting officer and authority (AO/AA). The AO/AA is also specifically tasked with the management, including the safeguarding and maintenance, of infrastructure assets.

Non-adherence to these responsibilities is likely to result in losses or fruitless and wasteful expenditure. Poor planning and inadequate project management cause project delays, late commissioning and the under- or non-utilisation of infrastructure assets.

In the infrastructure delivery process, there are usually two stakeholders: the client who requires the infrastructure and the implementing agent who implements the project on the behalf of the client. The budget normally resides with the client, who will therefore remain accountable for the spending of the allocated funds together with the implementing agent.

Audit outcomes demonstrate that in many cases controls over the infrastructure delivery process are not effective.

This typically results in the following deficiencies:

- Inadequate planning
- Late completion of projects
- Increase in budgeted cost
- Poor build quality
- Under- or non-utilisation of completed infrastructure assets

This guide on preventative controls in the infrastructure delivery process focuses on planning, project management, and commissioning and utilisation.

The guide includes limited detail on procurement. For more information on this part of the process, please refer to preventative control guide 4 issued in September 2020, which deals with the procurement of goods and services.

Oversight structures and executive authorities can use this guide to require assurance from the AO/AA that these preventative controls have been implemented and are working effectively – this is presented as questions to ask the AO/AA.

Ensure proper planning to reduce delivery delays and unnecessary costs

07

Controls accounting officers and authorities should implement

Institutions should properly plan infrastructure projects, by addressing the following key areas:

- Condition assessment of existing infrastructure
- Needs assessment and the consideration of alternatives
- Feasibility study
- Design development
- Pre-tender estimates
- Consideration of the best method of contracting included in the delivery and procurement strategy
- Availability of the appropriate site (including geotechnical investigations and environmental impact assessments)

Questions oversight structures and executive authorities could ask to obtain assurance

1. Has an infrastructure plan been developed and is it updated annually?
2. Have condition and needs assessments been performed as part of the planning process?
3. Has the AO/AA approved the infrastructure plan and any amendments thereto?
4. How is progress against the plan monitored, who is responsible for monitoring, and how are deviations from the plan dealt with?
5. Does the initiation of projects take place in accordance with the plan? If not, what actions are being taken to address any non-adherence?
6. Have stage-gate approvals been obtained before progressing to the next phase? In other words, are there control points at the end of a process where a decision is required before proceeding to the next process or activity?

Why it is important

Poor demand and procurement planning results in the inadequate development of specifications, wrong decisions about the type and scope of work and/or the feasibility of the project, and unrealistic cost estimates.

Controls accounting officers and authorities should implement

Institutions should have **adequate capacity and the required skills in place.** This means that:

- The tasks, roles and resources required for the infrastructure delivery function should be defined and the establishment should reflect the capacity required.
- The positions of key officials (namely the accounting officer, chief financial officer as well as chief directors and built environment specialists in the infrastructure delivery and/or project management office) should be filled and there should be a low vacancy rate in the infrastructure delivery management unit.
- The competence and skills requirements for officials should be defined in the relevant job descriptions. Recruitment should be done in accordance with these requirements. Any competency gaps should be identified and addressed through training and/or other development processes.
- The required competence and skills of other officials involved in the project management process (e.g. in the project management unit) should also be clearly defined and any gaps addressed.
- All officials involved in the project management process should be informed of, and trained in, the latest developments in the infrastructure sector, including all legislation, instructions, practice notes and guidance issued by the National Treasury as well as any other government and/or industry reforms.

Controls accounting officers and authorities should implement (continued)

Institutions should ensure that **infrastructure is completed timeously.** This means that:

- The contractor should commit to complete the project on time as per the approved contract,
- If the contractor is behind schedule:
    - the contractor should be put on notice
    - the contractor should submit a plan to get back on schedule
    - the institution should deduct penalties from progress payments
    - the institution should withhold part of the progress payment.
- If the contractor does not respond to the corrective action agreed to, notice of termination should be considered as a last resort.
- The project should be monitored regularly so that corrective action can be instituted early on and not only when the project is due to be completed.
- If necessary, the institution should call up the surety and retention money withheld to complete the project.

Institutions should ensure that **infrastructure projects are completed within budget.** This means that:

- The scope of the work (variation orders) as well extensions to the contract period should be managed where cost implications are applicable. This includes obtaining the relevant approvals from the client and/or relevant treasury.

Controls accounting officers and authorities should implement (continued)

- The client and implementing agent should comply with the contractual requirements and issue instructions and make payments for claims submitted on time as specified in the contract. This will ensure that claims for standing time and interest on late payments are prevented.
- Before progress payments are made, progress and materials on site should be verified.
- Institutions should ensure that infrastructure projects are built in accordance with design specifications and building standards to ensure that government is paying for **satisfactory standards of build quality.**
  This means that:
  - Project managers from the client and the implementing agent should conduct regular site inspections and monitor the contractor's workmanship.
  - Project managers from the client and the implementing agent should perform adequate verifications to ensure that design specifications and building standards are adhered to.
- Where deficiencies are identified, project managers of both the client and implementing agent should work together to craft a corrective action plan to hold the contractor accountable. The project should be monitored regularly so that corrective action can be instituted through out and not only at completion. Measures may include:
  - The contractor should submit a plan to improve quality.
  - The institution should call up the surety and retention money withheld to rectify the deficiencies identified.
  - The contractor should correct quality issues and rectify items on the snag list at their own cost. Retention amounts should be used when the contractor does not do so.
  - The contract liability period should be enforced and the cost of correcting latent defects should be recovered from the contractor.
  - If the contractor does not respond to the corrective action agreed to, notice of termination should be considered as a last resort.

Questions oversight structures and executive authorities could ask to obtain assurance

1. How have the number and the type of resources been determined for the infrastructure delivery management unit (including the project management unit)? Are these sufficient?
2. Is the position of the head of the unit filled? What is the vacancy rate in the unit? What actions are being taken to address vacancies?
3. Have the required competence and skills of every position in the unit been defined, and on what have these been based? What gaps have been identified and how are these being addressed?
4. Have the required competence and skills of other officials involved in the project management process (e.g. in the project management unit) been determined? What are the requirements for these officials?
5. Is there a specific training curriculum to ensure that officials understand and can apply applicable policies and procedures?
6. How is the training kept up to date with the latest developments?
7. How is it ensured that all new developments and reforms are communicated within the institution and that those responsible for implementation have been trained?
8. If there have been recent changes in legislation or new reforms, processes or controls by the National Treasury or provincial treasuries, questions can be asked specifically on how these were disseminated and implemented at the institution.
9. How are the time, cost and quality of the project continuously monitored? What actions are taken to address deviations?
10. Are variation orders and extensions approved at the designated level?
11. What steps have been taken against defaulting contractors (e.g. calling up sureties, retentions, or blacklisting)?
12. What action has been taken against professionals who signed off incomplete or poor-quality work?

Why it is important

Project management plays a major role in the construction of infrastructure. Adequate capacity and skills ensure that right decisions are made; correct processes are followed; and sufficient segregation of duties, supervision, review and monitoring are built into the overall project management process. New infrastructure is expensive and should have a long economic life span. Therefore, a quality product should be ensured to limit future maintenance and guarantee the safety of users.

When projects are not completed on time or at the required standard, it negatively affects service delivery to citizens.

Controls accounting officers and authorities should implement

The completed infrastructure should be commissioned and used upon practical completion, which will require cooperation between the implementing agent, client and other role players. This means that:

- Coordination between the implementing agent, client and other role players is necessary to ensure that the infrastructure can be commissioned and utilised immediately after practical completion. This means that resources have been procured and acquired to enable the commissioning process. It also means that other government institutions have been consulted to ensure that accessibility and commissioning of the infrastructure are enabled.
- Different phases of the project should be completed in a practical and logical order to enable testing to ensure that the project need has been met Where different role players are implementing different phases, there should be coordination to enable commissioning and service delivery.
- The guarantee/warranty period of equipment should be coordinated with the commissioning period of the infrastructure.
- After practical completion, the responsibility for the security of the infrastructure moves from the contractor to the client. Contracts should thus be in place to take over security responsibilities to eliminate vandalism and theft.
- Where applicable, training to beneficiaries should be conducted to ensure that infrastructure assets are used in accordance with specifications.

Questions oversight structures and executive authorities could ask to obtain assurance

1. Has commissioning taken place on the date as specified in the contract? What corrective action has been taken where commissioning has been delayed?
2. Have equipment, furniture, staff and other resources been made available for the commissioning of the infrastructure? If not, what corrective action has been taken?
3. Have multiple-phase projects been coordinated to ensure completion and commissioning in a practical and logical order to facilitate service delivery?
4. What security measures have been put in place to safeguard the new asset?
5. In the case of vandalism or theft, has timeous corrective action been taken to hold the responsible parties accountable?

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Why it is important

Service delivery to citizens is dependent on the timely commissioning and utilisation of completed infrastructure projects. In turn, such utilisation is dependent on the coordinated availability of the necessary resources.

Applicable legislation

Section 38(1)(a)(i) of the Public Finance Management Act (PFMA) states that the accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains effective, efficient and transparent systems of financial and risk management and internal control. Section 51(1)(a)(i) of the PFMA prescribes similar requirements for an accounting authority of a public entity.

The Treasury Regulations (TR) of 2005, issued in terms of the PFMA, requires the following relating to contract and expenditure management:

- TR 8.2.3: Creditor accounts must be settled within 30 days from receipt of an invoice or the settlement date or court judgement in the case of civil claims.
- TR 15.10.1.2: Sound cash management includes avoiding prepayments for goods and services unless required by the contractual agreement with the supplier.
- TR 16.7.1: The AA/AO of the institution that is party to a public-private partnership agreement is responsible for ensuring that such agreement is properly implemented, managed, enforced, monitored and reported on. Such AA/AO must also maintain mechanisms and procedures for:
    - measuring the outputs of the agreement
    - monitoring the implementation of, and performance under, the agreement
    - liaising with the private party
    - resolving disputes and differences with the private party
    - generally overseeing the day-to-day management of the agreement
    - reporting on the agreement in the institution's annual report.
- TR 17.2: Sets out retention periods for documents, including contracts and all other documents relating to the purchase of goods and services.

Applicable legislation (continued)

Section 6(1)(a) of the Municipal Finance Management Act (MFMA) determines that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the resources of the municipality are used effectively, efficiently and economically.

Furthermore, section 63(2) of the MFMA requires the accounting officer to take all reasonable steps to ensure that the municipality has and maintains a management, accounting and information system that accounts for the assets and liabilities of the municipality; and that the municipality has and maintains a system of internal control of assets and liabilities, including an asset and liabilities register, as may be prescribed.
These requirements are also applicable to municipal entities as per sections 96(2)(a) and 96(2)(b) of the MFMA.

Learn more about this control here

National Treasury website:

- Standard for an Infrastructure Delivery Management System
- Framework for Infrastructure Delivery and Procurement Management
- MFMA Circular No. 62 dated 20 August 2012: Supply chain management: Enhancing compliance and accountability
- SCM Circular dated 29 July 2011: Guidelines on the implementation of demand management
- Government Immovable Asset Management Act