

6TH NATIONAL PUBLIC SECTOR NON- COMPLIANCE AUDIT SYMPOSIUM

**VENUE: Southern Sun Elangeni Maharani Towers,
Durban, South Africa**

DATE: 08-09 MAY 2025

**THEME: THE TRUE COST OF NON-COMPLIANCE: HOW
MISMANAGEMENT TRIGGERS SERVICE DELIVERY
CRISES**

PRESENTER:

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PRESENTATION PLAN

1. HIGH LEVEL SYNOPSIS OF NON-COMPLIANCE AUDIT
2. UNDERSTANDING OF AUDIT OUTCOMES
3. ROOT COUSES OF IRREGULAR EXPENDITURE/ NON-COMPLIANCE
4. THE STATUS QUO OF SA MINICIPALITIES AUDIT OUTCOMES
5. **THE TRUE COST OF NON-COMPLIANCE-PUBLIC SERVICE DELIVERY CRISES**
6. WHAT CAN BE DONE?



HIGH LEVEL SYNOPSIS OF NON-COMPLIANCE AUDIT

- Public Audit Act,
- Public Finance Management Act of 1999 (PFMA)- **Financial governance of National and provincial governments**
- Section 38 (1) (a) (iii) of the PFMA-
- The Municipal Finance Management Act (MFMA)
- Billions of policies in place.
- Globally, annual loss on global construction procurement is USD 2,5 trillion through mismanagement, inefficiency and corruption
- R38,68 billion arose from breaches of legislation (A GSA2023)
- AGSA's (2023) report revealed **an ongoing financial mismanagement issue in local governments linked with poor service delivery and poverty.**
- In her presentation of the 2021-2022 and 2022/23 audit outcomes highlighted **financial mismanagement is a big hindrance to progress and provision of service delivery**
- Pervasive incidents of **non-compliance in many municipalities across South Africa.**
- Procurement challenges negatively affect service delivery and economic growth
- Mismanagement and poor government procurement lead to a **significant financial loss and poor service delivery** (Abdul Mateen, 2024; Fabra & Montero, 2023; Fazekas & Blum, 2021; Khalfan et al., 2022; Tinali, 2022).
- Financial Management and Compliance with legislation. Financial mismanagement and poor governance result in a wide failure to provide socioeconomic rights (Lisa Chormbortian, et al, 2021).
- The decline in service delivery (Madhi, et al. 2021)



UNDERSTANDING OF AUDIT OUTCOMES

- **Qualified audit opinion:** The financial statements contain material misstatements in specific amounts or there is insufficient evidence for the auditor to conclude that specific amounts included in financial statements are not materially misstated.
- **Adverse opinion:** The financial statements contain misstatements that are not confined to specific amounts or the misstatements represent a substantial proportion of the financial statements.
- **Disclaimer audit opinion:** there are insufficient appropriate evidence or documentation on which an auditor could base an opinion concerning the items reported in the financial statements.
- The lack of sufficient evidence is not confined to specific amounts or represents a substantial proportion of the information contained in the financial statements.
- **Financially unqualified or clean audit opinion-** financial statements contain no material misstatements.
- **Unqualified audits with findings**
 - **Three aspects:**
 - The financial statements do not have reportable material misstatements.
 - No material findings have been identified on the annual performance report.
 - There are no material instances of non-compliance with key legislation (AGSA 2023).
 - **Irregular expenditure:** expenditure incurred without complying with applicable laws and regulations (policies)- violations of the procurement-related provisions of the MFMA, PFMA (Auditor General,2024).
 - Correct procedures are not followed.



MEASUREMENT OF NON-COMPLIANCE

→ Irregular expenditure

→ Performance Management systems (KPIs on public service delivery)



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MAJOR CAUSES OF IRREGULAR EXPENDITURE

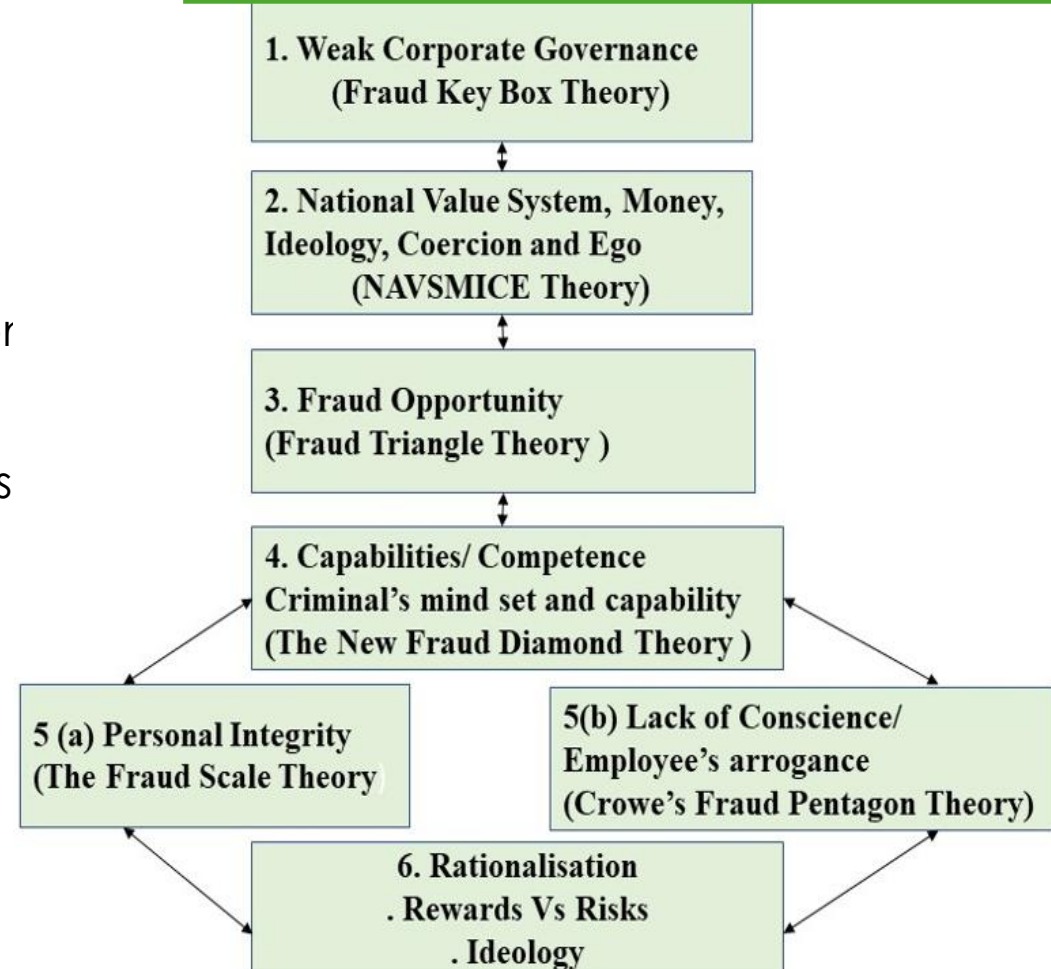
Irregular expenditure/Non-Compliance **violates**

- Public Finance Management Act,
- Treasury Regulations,
- The Municipal Supply Chain Management Regulation
- Municipal Finance Management Act,
- Municipal Systems Act, and the Public Office-Bearers
- Supply Chain Management Regulations/policies

86% of municipalities did not prevent IE (AGSA2023)

64% had material findings resulted from IE

→The New Fraud Combination Theory



CAUSES OF IRREGULAR EXPENDITURE

- WG:** Sound and effective corporate governance-preventative tool no matter how accessible the opportunity may be, or how strong the pressure or the rationale, ability, and capacity of the perpetrator (Ruankaew, 2016)
- NAVSMICE:** NAVS – National Value System; M = Money; I = Ideology; C = Coercion; and E = Ego (**Is the present National Value System in South Africa good or not good?**)
- FRAUD OPPORTUNITY:** Employee is presented with a chance to commit fraud, and he or she perceives that there is little or no possibility of being caught.
- Rationalisation:** employee feels justified in committing fraud (Risks versus rewards & Ideology).
- Fraudsters' mind set capabilities or competence:
 - Savvy enough to understand internal control weaknesses
 - Capacity to overrule or ignore IC/Accounting policies and other policies
 - Authoritative power
 - Fraudsters' intelligence and experience
 - Ability to deal with stress
 - Fraudsters are perfect liars
 - Capacity and ability to recognise the open doorway as an opportunity and take advantage of it by walking through it.

CAUSES OF IRREGULAR EXPENDITURE

6. **Fraudster's arrogance/Lack of Conscience-** Employee's belief that he/she is superior to others and that rules and regulations do not apply to him/her and his/her ability to override internal controls and exploit a situation to his /her advantage

7. **Personal Integrity: Rationalisation is not observable**

→ Personal integrity can be observed through **a person's decisions as well the decision-making process, taking ethics into account**

→ **Internal controls deficiencies**

→ **Corporate compliance deficiencies**

→ **Integrity deficiencies**



Pressure (non-shareable financial need):

- i. **The** first leg that motivates a person to commit fraud.
- ii. A severe financial problem may lead to a person committing an illegal act
- iii. **Financial Stability:** Threats to business financial stability
- iv. **Financial Pressure:** paying lifestyle, gambling etc.
- v. **Non-financial:** Lack of personal discipline and greed.
- vi. **Financial targets.**
- vii. **External and corporate Employment pressure**

MAJOR CAUSES OF IRREGULAR EXPENDITURE

Price quotations not obtained

Unfair and uncompetitive awards/bids

Abuse of emergency & sole supplier regulations

Awards without tax compliance declaration by SARS

Lack of monitoring of service providers

Failure to use preferential procurement regulations

Failure to procure from local producers

Conflict of interest – employees and

False declarations

Contract management

Composition of bid adjudication committees

Non-compliance with Construction Industry Development Board

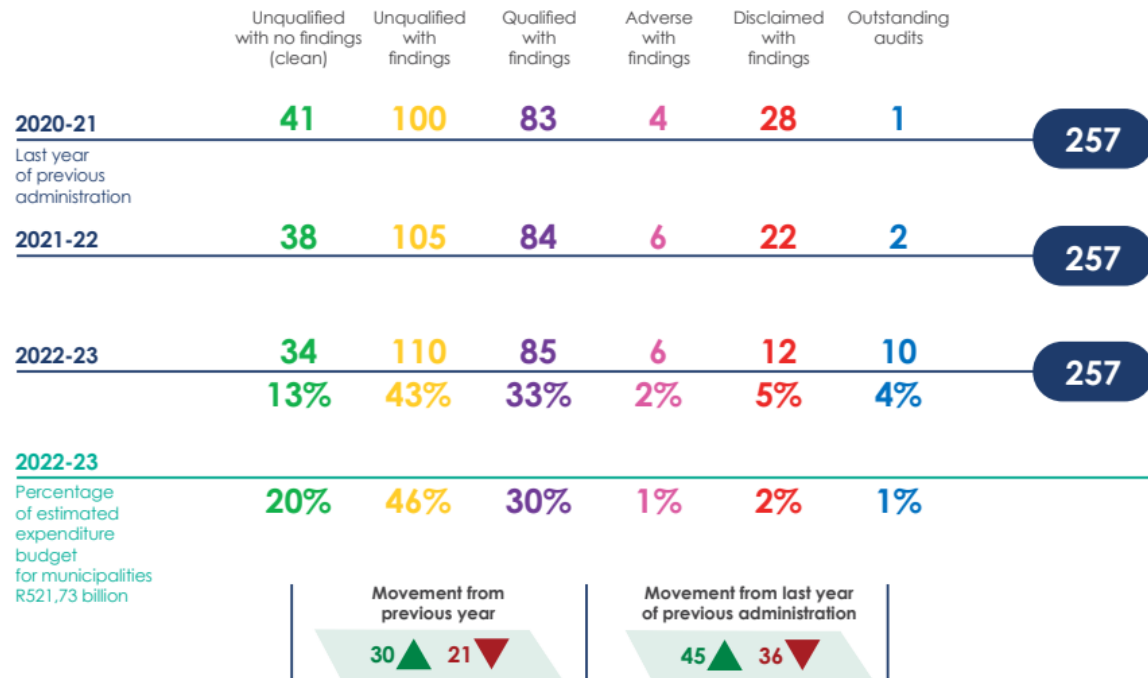
Lack of consequence management

Poor record keeping

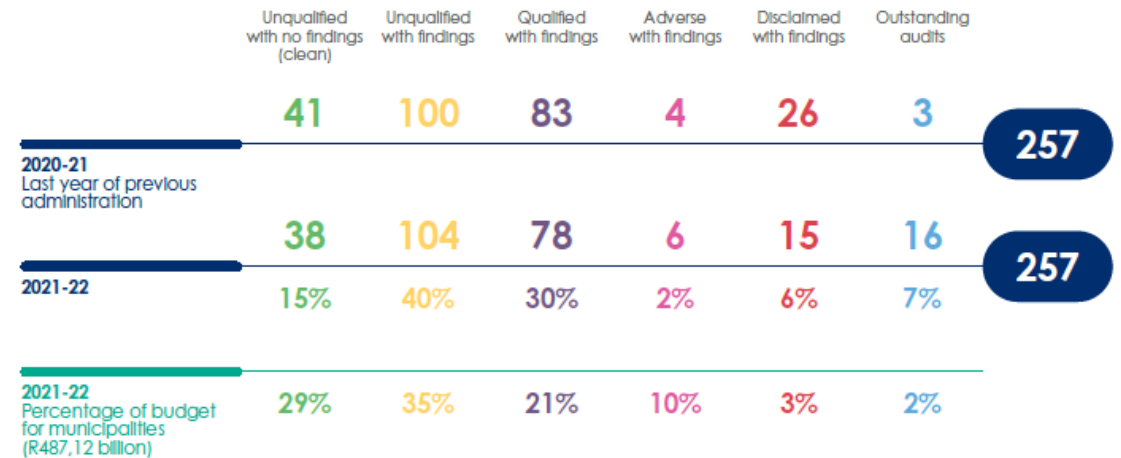
- Supplier chain management
- Poorly designed procurement contracts/**Procurement inefficiencies**
- Lack of ethical leadership
- failure to prevent irregular expenditure
- comply with SCM regulations
- **Tender irregularities that involve collusion between the officials and the service providers**
- **Politically deployed service providers will receive tenders**
- Procurement fraud/corruption
- Lack of accountability
- **Ineffective Municipal Public Accounts Committees (MPACs)- Failure if their oversight**

THE STATUS QUO OF MUNICIPALITIES AUDIT OUTCOMES

Audit outcomes – municipalities



Audit outcomes – municipalities



THE STATUS QUO OF MUNICIPALITIES AUDIT OUTCOMES

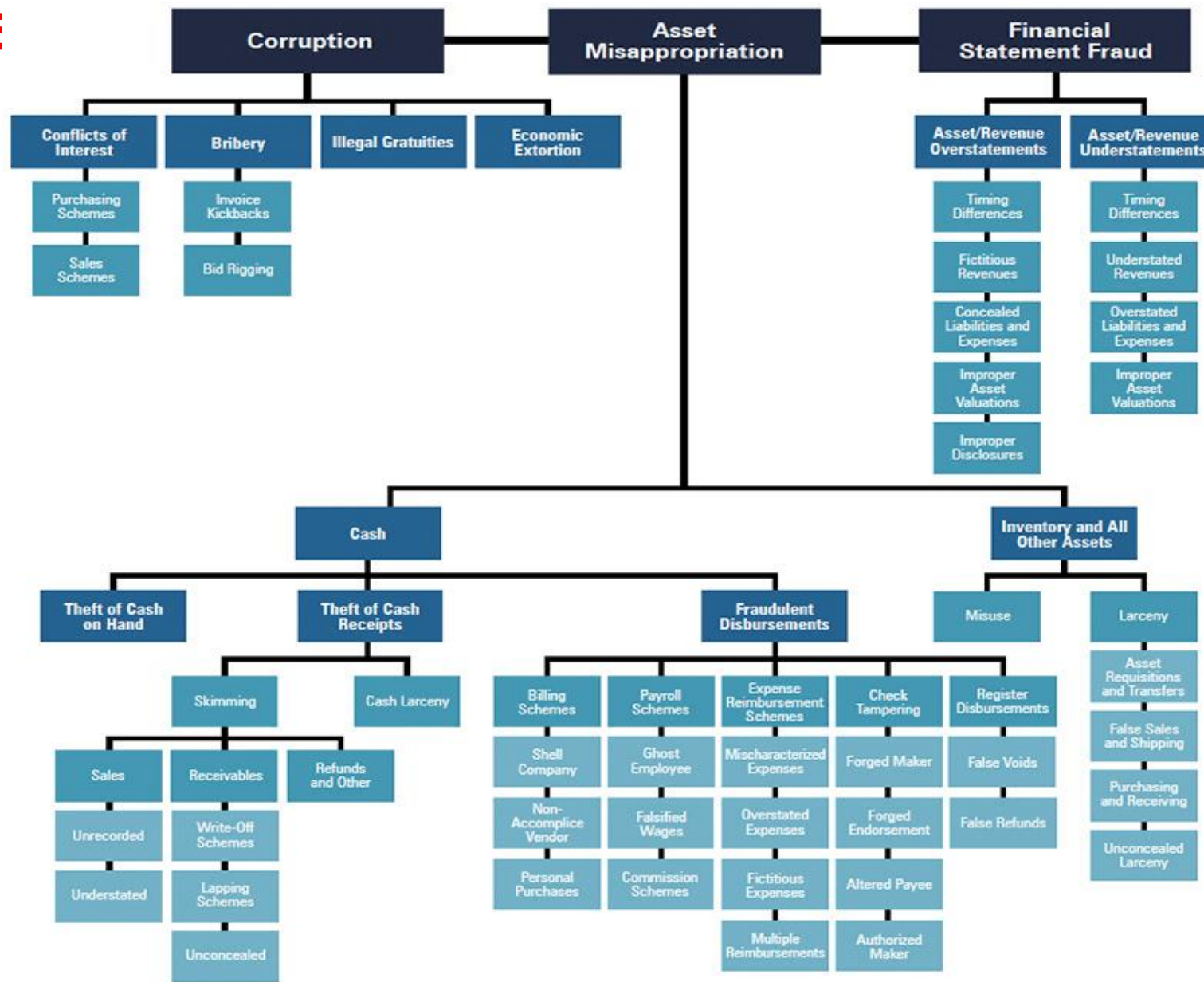
- Clean audits among SOEs continue to decline
- More SOEs lose this status, and others tend to move from unqualified to qualified audit opinions.
- The regressions are attributable to the general lack of maintaining the requisite level of compliance. (AGSA, 2022/2023).
- eThekweni is 1/8 metropolitan municipalities in South Africa (Its status on unqualified with findings remain unchanged for the past five years)

Movement in audit outcomes from 2018-19 – all auditees

	Unqualified with no findings (clean)	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Outstanding audits	
2018-19	93	177	98	3	28	0	399
Last year of previous administration							
2022-23	146	164	75	4	15	8	412
2023-24	142	168	58	4	5	38	415
	34%	41%	14%	1%	1%	9%	
2023-24	13%	57%	15%	2%	1%	12%	
Percentage of expenditure budget R2,07 trillion (operating and capital)							
Movement from previous year	58 ▲	44 ▼					
Movement from 2018-19	139 ▲	50 ▼					
Net improvement from 2018-19	89 ▲ (24%)						



THE FRAUD TREE



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THE TRUE COST OF NON-COMPLIANCE: FINANCIAL MISMANAGEMENT AND NON-COMPLIANCE & SERVICE DELIVERY CRISES

- Loss of public trust
- Vast increase/ Prevalence in protests of service delivery by communities and municipalities workers
- **Continual spikes in municipalities tariffs**
- **Delaying of service delivery/Disruptions in service delivery**
- **Increased costs of projects**
- **Poor access to clean water,**
- **Poor proper sanitation services,**
- **Inefficient transportation systems,**
- **Issue of electricity,**
- **Lack of maintaining roads and key infrastructures.**

- **Discourages/declines investment in local government**
- **Limits the ability of local governments to respond to community needs**
- **Disrupts governance structures**
- **Many unfinished projects in communities**
- Many municipalities' failure to execute their executive mandates
- They have been placed under section **139(1)(b) of the Constitution,** placing them **under the management of a Department of Co-Operative Governance and Traditional Affairs (COGTA) 's appointed Administrator**
- The inability to timeously pay their suppliers, huge and continuously growing debtors' books




THE TRUE COST OF NON-COMPLIANCE: FINANCIAL MISMANAGEMENT AND NON-COMPLIANCE & **PUBLIC SERVICE DELIVERY CRISES**

- Failure to meet key service delivery targets as per annual Service Delivery and Budget Implementation Plan (SDBIP).
- High bills for interest charges emanating from late payment of invoices, penalties from lawsuits,
- Inadequate infrastructure management practices/ mismanagement can lead to unsustainable service delivery, with high maintenance costs, frequent service disruptions, and a decline in the quality of life for citizens (Patience and Nel, 2021).



WHAT CAN NOW BE DONE?

- Developing adequate action plans to respond to Audit findings and recommendations
 - Based on the adage that prevention is better than cure. **Proactive techniques for fraud prevention, identification, and detection are strongly recommended rather than reactive techniques which favour the philosophy of “wait and see” or “repulse when attacked”.**
 - Municipalities should incorporate proactive fraud preventive, detective, and responsive measures.
 - Forensic audit functions should be created in NGOs to complement and supplement the work of internal controls in order to enhance the effectiveness of FRM within these entities.
 - Municipal leaders should display ethical steward leadership which generates high levels of commitment to deliver services to the communities.
 - **Political Competition and governance**
- 
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- Review and alignment of Internal policies and procedures to National Treasury regulations and guidelines on the implementation of the MFMA.
 - Assessment and Improvement of Internal Control Environment
 - Implementation of Consequence Management
 - surprise fraud audits to combat fraudulent activities
 - public-oriented and Society Centered
 - Servant Leadership Theory (SLT)
 - Municipalities in prioritising the citizen's needs, development, and welfare
 - **Easing the burden of poverty and delivering needed basic services to communities served by local municipalities**
 - **The use of Artificial Neural Networks (AI)/Auditing**

WHAT CAN NOW BE DONE?

Sustainability in Public Service Delivery

Sustainable service delivery ensures that municipalities can meet the needs of the current population while preserving the resources and infrastructure necessary to meet future demands (Daulat et al., 2024).

Public Value Theory

Public Value Theory, as proposed by Patience and Nel(2021), suggests that municipal managers are accountable for creating value for society by ensuring that public services meet the needs and expectations of citizens

Sustainable Development Theory:

Municipalities need to balance the present generation's needs with the ability of future generations to meet their own needs.

→ **Resource-Based View (RBV)** -local municipalities require careful management to maximise their potential for service delivery.

municipalities can provide sustainable services without overburdening public finances.

→ **Transaction Costs Economics theory:** How transactions between economics agents are organize and how associated costs are minimized Analyzing governance structures contractual relations within supply chains.

→ Procurement should be economic, effective and efficient

→ **The New Fraud Combination Theory**

- i. Incorporates all the elements of other fraud theories
- ii. Provides a strong foundation for the development of policies, strategies, and techniques to detect fraud in financial statements.



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