4.4 Financial Systems

Overview

Currently there are four major systems, the Personal and Salary Administration System (PERSAL), Basic Accounting System (BAS), Financial Management System (FMS) and Logistical Information System (LOGIS) that are maintained by the National Treasury for national and provincial departments. The various systems are managed as separate stand-alone "silos" and not as a single integrated systems unit. In addition, the national Treasury also maintains a Management Information System (Vulindlela).

Apart from these legacy systems, certain national and provincial departments have acquired a number of software solutions that are operated and maintained as separate "sub-systems". Over time, a great number of interfaces have been developed between the legacy systems and the "sub-systems" in a mostly uncoordinated fashion, following a process of "least resistance". (Currently, for example, there are more than 100 interfaces with BAS alone.)

The legacy systems within the national Treasury were developed as in-house proprietary solutions over a period of many years and in almost an evolutionary fashion.

The Financial Management System (FMS) is a cash-based accounting and batching system that was developed way back in 1973 and is now outdated. After a processing run, the expenditure data in FMS1 is carried over to FMS2, where the information is available on an on-line basis. It is, however, still functional in the Western Cape, Free State and KwaZulu-Natal provinces and at a few national departments. Currently, no enhancements are made to FMS and support is only focused on maintaining the system.

The Personal and Salary System (PERSAL) is the central system used for the administration of the public service payroll. PERSAL is very stable from a payroll perspective.

Over the years, PERSAL has expanded by increasing the spectrum of data fields to hold part of the information prescribed by national reporting requirements. In this respect, PERSAL offers personnel administration, holds information in a database of approximately 1,1 million employees, and offers standard and ad hoc reporting.

PERSAL was developed in an ad hoc fashion, with developments being mainly driven by legislative requirements rather than a Human Resource Strategy. New developments were therefore not informed by a systems life-cycle approach.

Salary payment and HR requirements are integrated into one system and therefore the database cannot be separated. The user focus is more on the salary function than on the HR function. The result is that HR data on PERSAL is neglected and often incomplete and inaccurate.

PERSAL interfaces manually with other systems (both internally and externally) through Magnetic Tape. An on-line interface with Vulindlela and other external systems is also in place.

The Basic Accounting System (BAS) is a basic accounting system (also cash based) that was developed in 1992 to cater for government's basic accounting needs. The architecture is more modern than that of the other systems and is assessed as being roughly in the middle of its normal systems life-cycle. The system is not a full-fledged accrual accounting system. It is only when the Accounting Standards Board makes the criteria known in respect of GRAP that one will be able to gauge whether BAS meets the specified requirements.

Some enhancements have been made to the system to accommodate the PFMA requirements. These enhancements mostly address "Commitments" and "Liabilities". The further advantages of BAS are a budget-blocking functionality that will make a significant contribution to limiting possible overspending, a cheque-release functionality that will assist in preventing cheque fraud, and a standard chart of accounts that will standardise and enhance reporting at all levels within government.

The Logistical Information System (LOGIS) in its current format was developed in 1998. LOGIS was developed in an evolutionary way to cater for government's provisioning and administration requirements in respect of the control of movable assets and stock.

The advantages of LOGIS include:

- Management of stock and stock levels (maximum and minimum levels).
- On average, a reduction of previous stock levels by a third (↓).
- Automatic reordering according to maximum/minimum stock levels.
- Automated inventories (movable assets).
- Commitment of all orders placed.
- Automated chief users.
- Automation of the provisioning environment.
- Availability of audit trails on all actions executed.
- Access and profile control.
- Availability of various detail and management reports, including the status of orders, goods received, inventories, store statistics, approved shortages, etc.
- Availability of a balanced scorecard which provides management with an internal service delivery, cost saving, improvement and financial perspective.

Even though LOGIS is not an asset management system, it complies with the provisioning administration processes and procedures and is an integral part of supply chain management.

The Management Information System (VULINDLELA) is a data warehouse that provides HR, finance and logistics reports. It relies on the PERSAL database and enhances access to reports, which offers high-level trends for management information.

On 1 April 1992 the Financial Management System (FMS) and Personnel and Salary Administrative System (PERSAL) were implemented on a centralised basis in the then Cape Provincial Administration (CPA). With the establishment of the province of the Western Cape on 1 July 1994, the centralised financial functions, including the administration of the systems, continued for all provincial departments, with the exception of the Department of Education, which managed its own financial functions.

As early as 1994 the devolution of financial functions to provincial departments to improve the quality of financial management and building capacity in provincial departments was identified as a priority by the Provincial Treasury.

However, it was not before the Public Service Act, 1994 (PSA) and the Public Service Regulations issued on 1 July 1999, whereby a provincial department was established as an autonomous entity, that the necessary impetus was provided to proceed with the devolution of financial functions. A further factor necessitating the devolution of financial functions to the departments was that the provincial Treasury could no longer be responsible for the day-to-day operation of the various systems on behalf of provincial departments and at the same time oversee the integrity of the systems (dichotomy).

To ensure that provincial departments have ample time to create the necessary structures and capacity to manage their own financial functions, the implementation and decentralisation of the FMS and PERSAL Systems commenced during the 1999/2000 financial year and was completed on 1 April 2002 in respect of the then ten provincial departments. The departmentalisation model, which was approved in June 2002, necessitated the further decentralisation of PERSAL and FMS to a further three provincial departments with effect from 1 August 2002. For further details of departmentalisation, see section 4.9.

In the latter part of the 2002/03 financial year, the Department of Finance and the provincial Parliament that have the necessary infrastructure and capacity potential will migrate from FMS to BAS.

Owing to outdated and insufficient systems that existed for the management and control of consumables and movable assets, the Logistical Information System (LOGIS) was piloted by the national Treasury and the provincial Treasury during 1999 at the Department of Agriculture. During the period 1 April 2000 to 31 October 2002, LOGIS was rolled out to a further 28 sites in the Province, with a further six sites to be implemented by 31 March 2003. By then it will manage a total stock value in excess of R1,2 billion.

As no standard Management Information System for the government as a whole existed, various software packages were utilised to provide management information. This was not only time-consuming but also provided outdated information in general. In cooperation with National Treasury, a Management Information System (Vulindlela) was developed and rolled out to 157 managers at head office level within provincial departments for increased access to relevant and up-to-date management information, enabling more effective decision-making.

As no standardised system existed to register losses, the Loss Control System was developed by the Department of Finance and implemented at all head offices of provincial departments. On 1 April 2000 the function was transferred to the provincial Treasury. As the system was developed for a centralised environment, the devolution of financial functions necessitated the redevelopment of the system to cater for the various component structures and delegations of provincial departments. Further development included availability of management information, improved response time and interdepartmental transfers of losses.

Current financial administration and management information systems

The following table illustrates the current systems in operation, the main functions of the individual systems, the main improvements effected since implementation and shortcomings that still exist.

SYSTEM	MAIN FUNCTIONS	IMPROVEMENTS	SHORTCOMINGS
Financial Management System FMS 1	• Cash-based system • Accounting transactions • Payments • Debtors • Bank reconciliation • Detailed miscellaneous and accounting reports	• Electronic fund transfers • Month close info available in electronic format • Enhanced debtors sub-system (includes age analysis) • Fleetman interface • Electronic downloading of reports • Debtor system further enhanced • User manuals available on national Treasury WEBSITE	• Not an on-line system • Allows for overspending on budget • Does not cater for General Recognised Accounting Practice (GRAP) • No standard chart of accounts
FMS 2	• Maintenance of code files • Budget capturing tool • Various management reports available (monthly and to date)	• User code/password revoke function • Operating system upgraded to link 17 • Identification of conditional grant objectives • Improved response time • Batch/payment enquiries • Cheque release functionality • Virement function available	• No on-line data-capturing facility • Not a budget system • No consolidated financial statements functionality available

SYSTEM	MAIN FUNCTIONS	IMPROVEMENTS	SHORTCOMINGS
Personnel and Salary System (PERSAL)	• Total human resource planning (Organisational structure and establishment administration) • Personnel administration: Appointments Promotions Terminations, Personnel development, service conditions and benefits • Salary administration: All types of payment of allowances and deductions and correct tax and fringe benefit calculations • Programmatical adjustment, i.e. salaries and state contributions of medical and housing allowances • Management Information: Various reports are available	• Caters for: • CORE • Magnetic tape interface for insurance companies • New resolution 7 leave dispensation • SMS packages • S&T claims to comply with SARS requirements • Access and profile enhanced • Enhancement • Interface with Government Employee Pension Fund • Introduction of "Entire" facility allows for transfer of data between Bureaus • Persal notices and manuals available in Intranet • Provides for reprint of IRP5 certificates and local printing • Skill development enhancements • The operating system upgraded to optimise performance (Sysphex) • Various reports available in electronic format • Verification of data with Home Affairs	• Does not cater for total personnel administration of educators • Does not optimally cater for certain control measures • Scanning facilities not available • Not Windows-friendly
Basic Accounting System (BAS)[1]	• Cash-based online system • Accounting Transactions • Payments • Debtors • Bank reconciliation • Detailed reports • Online enquiry • Maintenance of code files • Various management reports available • Budget-capturing tool available • Various levels of authorisation of payments	• Budget blocking • Commitments & liabilities • GG transport interface • Debit order interface • Budget Interface • Procurement/LOGIS interface • Standard chart of accounts	• Does not cater for Generally Recognised Accounting Practice (GRAP) • Not a full-fledged accrual accounting system • Scanning facility not available
Logistical Information System (LOGIS)	• Provisioning and procurement system • Control over consumables and movable assets • Provides for management information regarding stock and assets	• Managing stock by means of minimum and maximum stock levels • Over-stocking is minimised and predetermined as only a determined amount of stock can be held • Moving of assets is controlled • Availability of audit trails on all actions • Flexible infrastructure • Access and profile control The following functionalities are available:	• Not a financial budget control system • Does not interface up to minor item level • Not an asset management system • No BAR coding functioning • No BAS interface

1 The implementation of the Basic Accounting System (BAS) is scheduled for the latter part of 2002/03

SYSTEM	MAIN FUNCTIONS	IMPROVEMENTS	SHORTCOMINGS
		• Online printing • Guarantee register • Petty cash • FMS interface report • A4 order forms	
Management Information System (Vulindlela).	• Integrated management information • Drill down functionalities • On-line, printing and downloading functionalities • Information available at all levels • Relevant and up-to-date information • Standard reports available • Help function	• Web-enabled • In-year monitoring system • Monthly employment equity stats available on national WEB • Availability of PERSAL, LOGIS Information	• No access and profile control per institution • No management information on ledger accounts • Slow response time
Loss Control	Registration and management of all losses	• Interdepartmental transfer of losses • Availability of management information • Restructuring of application to enhance functionality and response time • Improved usage of component structures and delegations	• Limited consolidated data and management information available • Scanning facility not available

System Implementation

The Basic Accounting System replacing FMS will be rolled out to the remaining 12 provincial departments in a phased approach during 2003/04.

The Logistical Information System (LOGIS) will be rolled out to a further 20 self-accountable stores (health institutions) during 2003/04 and the remaining 15 self-accountable stores during 2004/05. This would increase the estimated stock value managed to more than R2,7 billion.

Vulindlela will be further rolled out to regional offices and institutions, subject to the necessary information technology infrastructure being in place and adequate to cater for the additional volume of transactions.

The Loss Control system will be rolled out to regional offices and institutions subject to the information technology infrastructure being in place and adequate.

Needs

A growing need exists for the interfacing and integrating of all financial systems. The following needs have been identified:

- A functionality that fully accommodates personnel administration of educators
- Optimal control measures in PERSAL
- Systems that cater for General Recognised Accounting Practices (GRAP)

- Budget control on LOGIS and PERSAL Systems
- Consolidated financial statements
- An appropriate budgeting system
- Management information on ledger accounts
- LOGIS to interface to minor item level
- An asset management system
- Barcoding
- Access and profile control on Vulindlela per institution
- Consolidated data and management information in Loss Control
- Scanning facilities in all systems
- BAS interface.

Way forward

Transversal issues

To further enhance the rendering of user support to users of the various systems, the National Call Centre System (LOGIK) will be implemented to enable the registering of all incoming calls, monitoring of outstanding calls and determining the service delivery level. Further, to ensure an uptime of at least 95% of all financial administration and management information systems.

The provincial system controllers (FMS, BAS, PERSAL, LOGIS and Vulindlela) in the provincial Treasury will represent this Province at the various National Forums, user meetings and workshops.

The provincial Treasury will, as assessed, issue the necessary Treasury Circulars, System Circulars/Notices regarding the effective, efficient and economical utilisation of the systems in all provincial departments.

Financial Management System (FMS)

On account of the high cost of maintaining two financial systems and the non-compliance of FMS with current requirements, the national Treasury has taken a policy decision to migrate all FMS departments/provinces to BAS in a phased approach by no later than 1 April 2004; to continue, for the interim, with the daily monitoring of the system so as to ensure that the available facilities (e.g. electronic transfers, financial authorities and commitments) are utilised to their maximum; that interfacing between the various systems (LOGIS, PERSAL, TELKOM, FLEETMAN, MEDSAS and official banker) occurs on a daily basis; that code files, access control and profiles are maintained.

These systems will be fully replaced by the Basic Accounting System (BAS) by 1 April 2004 (target date).

Personnel and Salary System (PERSAL)

The daily monitoring of the system to ensure that exception reports and ACB Limits are addressed; that computer-generated identification numbers are allocated only in exceptional cases and then replaced with a valid identification number within 90 days; that access control and profiles are checked on a regular basis; that computer-generated and unique reports are made available for management, budget, cash flow and monitoring purposes. A project will be registered for the verification of PERSAL data in all provincial departments and repeated annually.

Basic Accounting System (BAS)

As its implementation is phased in, migrating from FMS, the daily monitoring to ensure that the available facilities (e.g. electronic transfers, online enquiry and debtors) are utilised to their maximum potential; to monitor and ensure that interfacing between the various systems (LOGIS, PERSAL, TELKOM, FLEETMAN, MEDSAS and official banker) occurs properly five days a week; that code files, access control and profiles are maintained. BAS is to be fully implemented in all departments by 1 April 2004.

Logistical Information System (LOGIS)

The monitoring of the system to ensure that internal service delivery, cost saving and financial perspective of the 34 self-accountable stores on LOGIS comply with the national norms; that current and updated logistical information of movable assets and consumables is captured on the system; daily, that the available facilities (Balanced Score Card and reports) are utilised and followed up on a regular basis.

Developing and maintaining a digital catalogue (including photos), item description and item identification number of movable assets and consumables to enhance the procurement and provisioning process.

Management Information System (Vulindlela)

The daily monitoring of the system to ensure that Vulindlela is updated with the latest data from the functional systems (FMS, BAS, PERSAL, and LOGIS).

User requests are evaluated and forwarded to national Treasury for the further development of the system and/or the making available of additional information.

Loss Control

The daily monitoring and maintenance of the system to ensure that the facilities to register losses are utilised effectively. The further development of the system to provide for consolidated data and management information.

To be achieved

It is the aim to empower/assist the accounting officers in managing their revenue, expenditure, assets and liabilities within the limitations of the current systems. This will be achieved by promoting the effective utilisation of the financial, procurement and personnel systems. The ability of managers to access and interpret strategic decision-making data accurately and timeously will also be promoted, thus enhancing effective decision-making.

Further to this aim it is important to ensure that the decision-making data is up-to-date and that all available reports that reflect the data are utilised effectively. This data will be analysed to identify areas of risk and concern. These areas will be vigorously pursued with departments and corrective action will be enforced. If systems are utilised optimally, the Accounting Officer and Chief Financial Officer will be in a good position to prevent overspending.

The provincial Treasury forms part of the Technical Committee on Finance (TCF) work group, a sub-committee of the Budget Council, which will actively participate in finalising the TCF position paper on a management strategy in respect of an integrated financial management solution. It hopes to play a significant role in the planning, development, testing and implementation phases of the project. However, all stakeholders agree that the development, testing and implementation of a new Integrated Financial Management System will be a lengthy one, and there is a need to maintain and improve the current systems in the interim.

4.5 Supply chain management (Procurement and Asset Management)

Overview

The current systems of Procurement and Provisioning are fragmented owing to the fact that Tender Boards are at present responsible for procurement and provisioning, which is largely driven by norms and standards set by the national Treasury and partly executed within the framework of the Logis system. The division causes the current systems to be inefficient as far as the method of procurement, contract management, stock control and obsolescence planning are concerned.

Since the advent of the PFMA it has become increasingly important to reassess the functions of Tender Boards and their contribution to effective and efficient financial management within the provincial government. The value of the Western Cape Provincial Tender Board with regard to the processes of fairness, equitability, objectivity and impartiality is indisputable. However, as a result of the cumbersome procurement process and intricate chain of authority, unused funds at the end of financial years have forced departments to use these funds to acquire goods and services without taking into account the principles of effective buying, resulting in poor decision-making. Similarly, provisioning that is mainly driven by the Logis system is time-consuming and does not make provision for immovable property. The management of provincial immovable property, on the other hand, is governed by the Western Cape Land Administration Act, 1998, and is mainly the responsibility of the Department of Transport and Public Works.

It is imperative that a system be developed to eliminate fragmentation and integrate the manner in which procurement and provisioning is being dealt with. Therefore, firstly the Western Cape Provincial Tender Board is being restructured and it is envisaged that it will be replaced by a supply chain management Advisory Council that will, among others, have the following functions:

- promotion of fair, equitable, transparent, competitive and cost-effective supply chain management;
- monitoring and reporting on the fairness, equitability, transparency, competitiveness and cost-effectiveness of supply chain management;
- advising the Minister of Finance on the fairness, equitability, transparency, competitiveness and cost-effectiveness of supply chain management;
- acting as a body of appeal.

Secondly, the responsibility and accountability for procurement and provisioning will be gradually devolved to accounting officers. Thirdly, the provincial Treasury will effectively perform the functions concerned as set out in section 18(c) of the PFMA.

It is recognised that the abovementioned “procurement model” will best serve the interest of the provincial government. Procurement is a powerful tool in the hands of government, and if used more strategically and effectively, a greater number of socio-economic goals, as identified in the RDP, can be achieved. Thus, by developing best practices and procuring in a better, smarter, faster and more cost-effective way, procurement can be used to directly target SMMEs and, among others, enhance the participation of historically disadvantaged individuals (HDIs) in provincial procurement.

In order to achieve this and thereby establish a sensible way forward, a common thread must be sought between procurement and provisioning. This is done by moving towards the process of supply chain management. Supply chain management forms an integral part of Financial Management and introduces international commercial best practices. It seeks to bridge the gap between traditional methods of procuring goods, services and property, stock control and obsolescence planning whilst at the same time addressing procurement-related matters that are of strategic importance.

Supply chain management starts of with the process of demand management and acquisition management that in effect constitutes the procurement process and then moves into the next phase, which is logistics management (in effect provisioning). It finally concludes with the process of disposal management that constitutes the disposal at the end of the useful economic life span of an item and ends the cycle with a performance or **value for money** assessment phase. In practise these phases run concurrently as different items have vastly different useful economic life spans.

The fact that there is no integrated process or strategy with regard to the acquisition, control and disposal of provincial goods, services and property poses the question whether the provincial government is utilising the resources at its disposal to its maximum benefit. The introduction of Public Private Partnerships will be an important tool to improve infrastructure and service delivery efficiency and will bring about a new approach in the optimal utilisation of state resources.

In addition, government's priority is to meet the socio-economic needs of all South Africans and in particular to alleviate poverty. The challenge will therefore be to use procurement as a tool for economic development. The introduction of the concept of black economic empowerment within the supply chain management process is essential for providing more economic opportunities to those historically disadvantaged and therefore seriously facilitates meaningful and sustainable empowerment.

Central to the aforementioned is the budgetary capacity of the provincial government, which will always be a factor that needs to be taken into account. A balance must therefore be struck between affordability and the pursuit of socio-economic objectives. It is important that the provincial government tap the wealth of innovative and specialist skills that is available in the private sector to complement their budgetary capacity to meet the challenge of effective and efficient procurement of goods, services and property whilst ensuring that this process also addresses socio-economic issues.

Procurement

The current system of procurement is rule-driven and it is debatable whether or not it constitutes value for money. It also limits procurement personnel in coming up with innovative procurement practices. The rule-driven approach stems from the fear of unfair practices and the introduction of punitive measures where such rules have been broken. As such it has created a procurement environment in which emphasis is placed on the adherence to rules and minimising possible irregularities instead of encouraging smarter and better procuring and having a more entrepreneurial approach to buying. Procurement personnel in the government are performing procurement administrative functions rather than buying functions. The current system of procurement also has the following inherent risks:

- The different markets and their specific requirements are not fully understood.
- Needs/Requirements of departments are not properly addressed and therefore not clearly defined and specified.
- Bid/tender documents are not prepared effectively.
- Proper cost and benefit analyses are not being done.

The knowledge of procurement personnel is mainly confined to legislation issued by the Western Cape Provincial Tender Board. Limited contract management skills exist, creating unnecessary budgetary pressures due to the inability to deal adequately with contract price adjustments and rates of exchange claims. Limited knowledge of the legality of contracts also extensively increases the Province's risk of possible litigations arising from the conclusion of contracts.

These factors are of concern if it is taken into account that procurement expenditure forms a substantial part of the provincial budget. It is also one of the few areas of considerable discretion whether to spend and on what. As such it should be a high-focus area to ensure that departments stay within their budgets.

The amount spent by the Western Cape government in the 2001/02 financial year through the procurement process is depicted below:

Department	Amount R'000
Premier, Director-General and Corporate Services (PAWC)	180 756
Finance	10 519
Community Safety	20 668
Education	271 397
Health	861 483
Social Services	87 023

Planning, Local Government and Housing	13 814
Environmental Affairs and Cultural Affairs and Sport	39 573
Economic Affairs, Agriculture and Tourism	862 444
Grand Total	**R2 347 677**

These amounts were mainly spent on the following:

Industry/Sector	Amount R,000
Agriculture, Hunting, Forestry and Fishing	81
Mining and Quarrying	2 035
Manufacturing	522 846
Electricity, gas and water supply	77 185
Construction	239 154
Wholesale and retail	417 589
Transport, storage and communication	518 875
Financial and Business Services	386456
Community, social and personal services	181 375
Private house and other activities	2 081
Total	**R2 347 677**

Efficient, effective and economical procurement of goods and services becomes more important if it is taken into account that it is the intention of the provincial government to use it as a tool for economic development, with specific emphasis on the development of small, medium and micro enterprises and increasing the participation of historically disadvantaged individuals in provincial contracts. With regard to the latter, various initiatives were spearheaded over the last couple of years, with the 10 Point Plan Strategy, the Green Paper on Public Sector Procurement Reform, 1997, the Preferential Procurement Policy Framework Act, (2000) and its Regulations (2001) being the most important. These documents established the concept of Preferential Procurement in government service. Although preferential procurement was, to a limited extent, introduced in 1998 in the provincial government, it only took shape with the introduction of the Western Cape Preferential Procurement Policy on 1 January 2002 and the institution of Departmental Plans for Preferential Procurement.

As a result of the introduction of preferential procurement, historically disadvantaged individuals are slowly starting to play a meaningful role in the Western Cape government's procurement environment. Contracts to the value of R207 million and R238 million in the 2000/01 and 2001/02 financial years respectively were awarded to historically disadvantaged individuals. These, however, are not sufficient to facilitate meaningful participation and broaden the economic base. The Minister of Finance and Economic Development therefore directed that at least 40% of the value of provincial contracts awarded needs to flow to historically disadvantaged individuals. As such, departments were requested to reflect their "procurement budget" and the amount earmarked for preferential procurement for the 2002/03 financial year. Preliminary indications are that contracts awarded to historically disadvantaged companies for 2002/2003 will be ± R350 million, which is a substantial increase compared with the previous years.

However, cognisance should be taken of what has been experienced since the full introduction of preferential procurement on 1 January 2002. The concept of preferential procurement has not been fully embraced as the opinion was held that, **firstly**, it would create a burden on the budget, **secondly**, that it would bring complexity to the procurement process, and **thirdly**, that the skills needed to build it into bid/tender documents were inadequate. Further to that, there was a lack of clear strategy at national and provincial levels on how to deal with and effectively implement this concept.

Nevertheless, there is a clear indication of the possible impact of preferential procurement in the provincial procurement environment. Apart from the health and roads construction industries, the province can make a substantial impact on companies owned by HDIs. Within the health industry it was found that HDI companies range from few to non-existent. This is mainly because of the structure of the health industry and the various laws in place governing health products and services. Most of the health products/services are imported and supplied by multinational companies and entry to this market requires a fair amount of capital.

Simultaneously, entry to the roads industry is not easy owing to its complexity and technical nature. In both the aforementioned industries, and others to a lesser extent, it is quite clear that preferential procurement based solely on equity of companies will not bring about the necessary change to facilitate meaningful participation by HDIs, and that other initiatives will have to be pursued. These initiatives would include the promotion of joint ventures between the more established companies, on the one hand, and HDIs and small and emerging companies on the other. A component of such joint ventures will need to be an adequate skills transfer, be it management or technical.

Although the initial aim of preferential procurement is to broaden the economic base and to empower those disadvantaged, there are certain allegations and evidence of possible abuse by established businesses that change their shareholding but not the management structure of their companies so as to take advantage of the system. Likewise, there are allegations that “black” companies obtaining contracts “sell” these to the more established companies. The aforementioned practices are certainly not in the spirit of the Preferential Procurement Policy Framework Act, and if found to be true, strong punitive action should be instituted against offenders.

Public Private Partnerships

Public Private Partnerships (PPPs) are an integral component of the state’s overall strategy for the provision of public services and public infrastructure across all sectors. This does not imply that PPPs are the preferred option for improving the efficiency of service delivery, but rather that they enjoy equal status among a range of possible service delivery options available to departments in all spheres of government.

Infrastructure development through the procurement process, especially through a public private partnership initiative has long-term contractual commitments in mind. However, it must be affordable, provide good value for money and transfer appropriate technical, operational and financial risk to the private sector party. Limited experience with regard to PPP initiatives, specifically those entailing private finance, has produced mixed results. However, if correctly structured, PPPs are a useful service delivery option from both an operational and a strategic perspective.

Existing procurement legislation and regulations are, however, geared to conventional procurement activities, as for civil works construction and the purchase of equipment and services. Existing procedures are neither designed to address the complexities of PPPs nor do they provide a basis for ensuring that the key dimensions (e.g. affordability, value for money and efficient risk allocation) are appropriately evaluated.

Ensuring effective service delivery through PPP arrangements typically requires additional functional capacity in financial, technical and managerial areas that is not normally associated with the operation of a government department. Moreover, while it could be argued that government officials have developed skills as contract managers for simpler forms of PPP arrangements, such as service and basic management contracts, this is not true for more complex PPP contracts. The requisite skills for long-duration contracts that entail significant risks are still in relatively short supply in the public sector and will have to be developed over time. A balanced approach is therefore required, both to build the required capacity and to reduce the demand on capacity, for example, by adopting measures that reduce the complexity of PPP arrangements.

Opportunities for potential PPPs within the Western Cape government and the need to build capacity must still be explored. The Province has identified projects for the nature reserves in the Western Cape, hospitals and clinics, and toll roads, of which the Chapman's Peak Drive is the most advanced PPP thus far. However, the constraints that the provincial government faces are no different from the constraints identified in the national Treasury's Strategic Framework.

Apart from the latter, however, the provinces have inherent constraints that only they themselves can remove, eliminate or find solutions for. Some of the constraints include, among others, the following:

- The PPP unit of the national Treasury and the provincial treasuries needs to build the necessary capacity for the identification and managing of PPPs.

- Treasury Regulations vest all the powers for the approval of PPPs with the national Treasury. Provincial treasuries' role at this stage is undefined and the rules are written in such a way that provincial treasuries can easily be bypassed with the conclusion of a PPP agreement. This can result in unmandated guarantees being imposed on provincial treasuries.
- Provincial treasuries cannot conclude or give authority for the conclusion of a PPP transaction until such time as the national Treasury has given accreditation to a province to do so.

Another potential constraint is that provincial treasuries do not have a dedicated unit to identify and pursue potential PPPs. Should such a unit be established, it would require access to departments to identify potential projects. Apart from that, it would also require greater coherence and cooperation within the provincial Treasury to clear contentious aspects such as the directing of revenue generated by the PPP project and confirmation that provision has been made for related expenditure during the MTEF period. Furthermore, since PPPs normally stretch over longer periods than the MTEF period, suitable budget provisions need to be developed to incorporate expenditure related to PPP agreements.

The level at which PPPs are being pitched are high and indeed rightfully so when looking at the amount of skill that is required to conclude long-term agreements that must stand the test of time in a dynamic legislative and economically sensitive environment. Provincial treasuries must give attention to this aspect and need to develop mechanisms to guide departments. Notwithstanding this, departments must continue to identify possible areas which can be best served via the PPP process.

Asset management

Under the PFMA, accounting officers will be required to compile a balance sheet. Part of that balance sheet will be departmental assets, the management of which is currently covered by Treasury Instructions that are highly prescriptive in terms of both record keeping and procedure.

The current system of procuring goods for departmental use, storing it, accounting for it, and providing it to end users, can best be described as cumbersome. It is probably also very expensive but there are no readily available figures to determine the costs of storage space or the costs of staff and equipment that operate a store. The staffing components in a typical store comprise of: accounting (the paperwork); warehouse (physical storage, issue and receipt notes); transit (checking for quality and quantity); and a limited amount of distribution (delivery to end users).

The summarised process is:

(a) an end user places a request on the store for an item;

(b) the store draws it from stock or, if not held in stock, places an order under a period contract, or seeks quotes, or goes out on tender depending on the money value of the order;
(c) the item, if placed on order, is received into store;
(d) the end user collects the item or it is delivered.

A computerised mainframe-based logistical system (LOGIS) has been developed by the national Treasury over the last decade to try to provide a form of store administration, to monitor stock levels and generate procurement needs, and to provide asset management that is compliant with current Treasury Instructions. LOGIS is not seen to be user friendly, is difficult to comprehend and to operate, and so far has only been installed in limited sites. Many departments are still operating on manual systems, which are very labour intensive. The national Treasury is therefore seriously considering stopping any further enhancements and further roll out of the Logis system.

The databases and the asset and inventory control functions on Logis have some value and should be maintained. Until such time as finality is reached on the life of Logis, the implementation of Logis within institutions in the Western Cape will proceed as planned.

Acquisition and disposal of immovable property

The acquisition and disposal of provincial immovable property also needs to be done with the utmost care and in a transparent manner. From a financial perspective, property represents capital expenditure and wise and careful consideration of such expenditure is required. Property is considered an asset which, in future, may provide a major part of provincial accreditation for accessing loans. Property may also be a productive asset in that it generates additional revenue for the Provincial Revenue Fund.

The usage of provincial properties (land and buildings) needs reviewing in order to ascertain whether or not the properties are in fact being utilised to their optimum. Property is also used in support of socio-economic development. Providing suitable accommodation to client departments dealing with socio-economic matters could contribute towards this. This is done by allocating to the needy and previously disadvantaged individuals and groups suitable premises in order for them to undertake business initiatives. Once again, a demand-driven approach is followed whereby needs are identified and then related to individual properties. The provincial government has already approved a Green Paper for the Management of Provincial Properties in the Western Cape. One of the major recommendations in the Green Paper is the establishment of a Provincial Strategic Accommodation and Infrastructure Plan for the Province. This plan will address the accommodation needs of the Province and redundant properties, and properties that are not needed for the short-term will be identified and can be used for other than provincial users. The eventual White Paper will also address the best use of properties to ensure that they can be utilised for redressing the past as well as making money for the Province to utilise for the maintenance, upgrading or acquisition of properties for the Provincial Property Portfolio.

This White Paper is now in its final stage.

Socio-economic development may also be obtained through utilising individual properties for land restitution purposes. This is not a provincial demand-driven function, but individual provincial properties may become involved. In this instance, therefore, an individual property-driven approach is followed whereby the property determines the action.

In addition, property has the potential to generate income for the Province and its people. Properties with possibilities for business promotion and the generation of revenue for the Province will support economic development and socio-economic development through job creation. Small, medium and micro enterprises (SMMEs) as well as historically disadvantaged individuals and groups will be supported when competing for the utilisation of such properties. Obviously, the additional revenue generated can be redirected into socio-economic development by providing more accommodation to be utilised for that purpose.

As with the procurement of goods, services and property, the disposal of any asset of the Province needs to run through the whole supply chain management process.

Black economic empowerment

Over the past number of years, government has initiated a number of strategies over a broad front to bring about structural change in the economy. In all government programmes, the extent to which black people benefit is a fundamental criterion of operation and success. This has consequently resulted in actions and policies that will have the effect of bringing about black economic empowerment in many spheres of society and the economy.

Government, by introducing the then 10 Point Plan Strategy on Procurement and the Preferential Procurement Policy Framework Act, 2000 and its Regulations, 2001, has endeavoured to promote black economic empowerment (BEE).

Notwithstanding the above, economic power is mostly still in the hands of the few and economic performance overall is still disappointing. The anticipated transfer of ownership to the black majority has not materialised, trapping most in a vicious cycle of extreme poverty, unemployment and underdevelopment. The perception persists that racial inequality remains fundamentally ingrained across all sectors of the business community. This is a structural impediment that continues to distort the efficient functioning of markets in South Africa and reinforce marginalisation, rather than promoting viable and sustained economic participation.

It would appear that the manifestation of low levels of economic participation, especially among young and female South Africans, is due in part to the combined effects of institutional barriers, uncompetitive markets, and inadequate information about job opportunities.

The challenge facing South Africa dictates a fundamental change in approach in all sectors of society, particularly in established business. There should be a sustained effort to mobilise all South Africans to arrive at national consensus on the priorities of economic transformation and the roles and obligations of all stakeholders in helping achieve these objectives. This, by definition, has to be a State-driven programme. Markets tend to reinforce an existing distribution of incomes and assets. This is unacceptable in a country such as South Africa, where the market mechanism was deliberately distorted to allocate incomes and assets on non-price criteria such as race. The private sector needs to recognise its collective responsibility to invest in the country and assist government in achieving development goals. The private sector should be encouraged to take into account private and social returns and factor longer-term and strategic considerations into investment decisions. This is an inclusive process and its outcomes are for the benefit of the whole nation and future generations.

Needless to say, the immigration from the existing to the ideal situation will require national and associated provincial strategies which will probably take about 10 years to come to fruition. However, one should not lose sight of immediate interventions that should be put in place to strengthen such a national stategy.

Government procurement has long been identified as a strategic tool to ensure that certain socio-economic goals are attained. The estimated R60 billion spent by the local, provincial and national spheres of government has therefore over the last couple of years been targeted to a large extent to increase the participation of black businesses in government contracts. Unfortunately no meaningful data exists to establish the contribution of these spheres of government.

The Western Cape government's overall expenditure on procurement is R2,3 billion, and although it is relatively small in the national context, one should not underestimate the value that it can add to black economic empowerment. However, it is imperative that one should have a deeper understanding of the Western Cape economy to identify its dynamics, backward and forward linkages, constraints, enabling factors and skill requirements to promote black economic empowerment.

Way forward

The aforementioned paragraphs illustrate the fragmented approach within which government resources are being utilised. As mentioned earlier, a common thread must be introduced to integrate these processes so as to form one process referred to as supply chain management, which will seek to bridge the gap between traditional methods of procuring goods, services and property, stock control and obsolescence planning, whilst at the same time addressing procurement-related matters that are of strategic importance.

The key to supply chain management is the introduction of the value-for-money concept, of which the following requirements are an integral part:

A total needs assessment dealing with -
- an understanding of future needs and making provision for it in the MTEF;
- the identification of critical delivery dates and the frequency of needs;
- the determination of proper bid specifications addressing the relevant needs and not a specific product or service in the market.

The development of proper documents fully addressing:
- preferential procurement requirements;
- the strategy on how to approach the market;
- the concept of total cost of ownership, including life cycle and inventory carrying cost;
- bid evaluation in criteria, how bids will be evaluated and how contracts will be administered and managed.

Proper logistical management, including -
- the coding of items and setting of inventory levels;
- placing, receiving, expecting and distributing national warehouse management orders;
- transport management and supplier performance.

Obsolescence planning to achieve the best returns for the Province by -
- maintaining a database of materials and redundant stock;
- determining the economic life of an item;
- determining the best possible disposal strategy.

Each phase of this concept, as depicted above, requires its own set of standards, some regulated by the national Treasury, the rest in a cascading manner by provincial treasuries, accounting officers and accounting authorities, as provided for by the PFMA and other supporting legislation respectively. Apart from acquiring the systems, building the capacity in departments, schools and public entities, making sure at least of nominal compliance with any prescribed standards (regulations) and developing the substantive standards (benchmarking, including practice notes) to effectively roll out this new concept of achieving value for money throughout the supply chain management cycle, implies a whole set of new challenges for provincial treasuries.

The challenge within the provincial government will be to transform the existing rule-driven and fragmented way in which procurement and provisioning (assets) are currently being dealt with. Systems need to be put in place that can generate the management information needed for sound financial and economic decision-making. Current personnel need to be re-skilled and/or adequately skilled personnel should be recruited to drive supply chain management within the provincial government. The provincial Treasury needs to increase its capacity with regard to proper contract management, black economic empowerment initiatives and public private partnerships. In addition, they need to put the necessary policy and monitoring mechanisms in place to assist departments to achieve the provincial Government's goals with regard to black economic empowerment.

The ability of the historically disadvantaged to take advantage of the economic opportunities presented by an expanding economy must be increased. The contribution of R2.3 billion (provincial procurement) is relatively small compared with the Western Cape's GGP, and although it is not significant enough to change the structure of the provincial economy, it will create opportunities for BEE companies to get a foothold in the economy and to benefit from the multiplier effect. The reallocation of expenditure to BEE companies will have a significant impact on stimulating growth and job creation. It is, however, important that further research should be undertaken to identify the inhibitive and promotive factors for BEE in order to establish successful models which could be emulated by the private sector.

Creating opportunities for BEE companies will, however, not be enough. The provincial government will need to decide to what extent it will provide additional support, which will include hand-holding and access to finance, to BEE companies to ensure that they play a meaningful role in the Western Cape economy.

4.6 Cash management

Overview

After this country's first democratic elections in 1994, the new provincial dispensation was constituted. Similarly, the functions pertaining to the high-priority task of cash management were devolved to the provincial treasuries. This meant that the provinces would be solely accountable for their financial position, thus ensuring that the unique needs of each province could be served. Accordingly, the Western Cape Exchequer Law, (Law 4 of 1994), stipulated, inter alia, that a prescribed banking account configuration should be held at a commercial bank.

On 1 April 1995, a Provincial Exchequer Account and two Paymaster General accounts were opened, viz. the Department of Education and a single account "Other Departments" to service the needs of the remainder of the departments within the provincial government.

On 1 July 1999, amendments to the Public Service Act, 1994 (PSA) and the Public Service Regulations, 1999, were effected, which devolved considerable powers to executing authorities (national and provincial), and established provincial departments as autonomous entities, which provided for the further devolution of financial functions to the departments. The Public Finance Management Act, 1999, (Act 1 of 1999), as amended, applicable with effect from 1 April 2000, which has as its main objective to secure accountability and sound management of the revenue, expenditure, assets and liabilities within government spheres as a whole, was instrumental in permitting the decentralisation of cash flow management to the various provincial departments.

In terms of this policy of decentralisation, a Paymaster General Account has been opened for each of the thirteen provincial departments. This has contributed largely to effective cash flow management in the provincial government.

Legal Framework

- The Constitution, 1996
- The Public Finance Management Act, 1999 (Act 1 of 1999)
- National Treasury Regulations
- Provincial Treasury Instructions
- Western Cape Exchequer Law, 1994 (Law 4 of 1994)
- Direct Charges Act, 2000 (Act 6 of 2000)
- Division of Revenue Act, 2002 (Act 5 of 2002).

Mechanisms

The source of this Province's funding originates mainly (94%) in the national Treasury by way of the payment of an equitable share and conditional grants, whilst the remainder is sourced from provincial own revenue such as motor licence fees, hospital patient fees and gambling taxes. The national share is transferred to the Province on a weekly basis by means of an electronic funds transfer into the Provincial Exchequer Account, which is the accredited account of the Province into which all revenue flows. These transfers are credited in terms of a payment schedule, which is made available by the national Treasury prior to the commencement of the financial year and reflects the total allocation originating in the national Treasury. A unique bookkeeping system, which does not form part of the transversal financial systems used by government, is maintained which records all income and expenditure pertaining to the Provincial Revenue Fund, to ensure accountability and an accurate audit trail. Each provincial department within the provincial government provides the provincial Treasury, prior to the commencement of the financial year, with estimates of revenue and expenditure for the following financial year, which facilitates the cash management process. Each departmental Paymaster General Account is funded on a daily basis from the Provincial Exchequer Account in terms of daily cash flow inputs from the various departments. The cash management system of the provincial banker, to which the province has a direct link, is utilised to perform such electronic transfers. Once the daily cash flow has been finalised, any moneys which are not immediately required to defray expenditure are invested at financial institutions, in terms of an internal investment policy. At any given time, the Provincial Revenue Fund experiences a temporary accumulation of funds as a result of “delayed payments”, i.e. orders that have been placed, but in respect of which, owing to delivery periods, the necessary invoices have not yet been received and payment therefore has not been made.

Challenges

The ever present challenge with regard to cash flow management is the continued striving for improvement and refinement of the various planning and work procedures, utilised to perform the tasks related to this function, which will culminate in the enhancement of effective cash flow management in the Province.

The training of the relevant officials within the provincial departments in so that they can provide the provincial Treasury with accurate cash flow information on a daily basis is a further challenge. This will greatly improve cash flow management.

The envisaged cash flow model, which the national Treasury is considering implementing within provincial governments, will result in a new working environment, thereby presenting fresh challenges with regard to cash flow management.

In order to increase provincial revenue by means of interest on investments, optimum interest rates must be obtained from financial institutions, taking into account the maximum exposure to these institutions, associated risks and investment periods.

The ultimate challenge, however, is to ensure that, on the one hand, the accounts within the provincial government remain minimally cash positive on a daily basis and, on the other, that no overdrawn situation occurs at any time.

Fiscal adjustments (Risk management)

The national Treasury may amend the monthly percentage attached to the payment of the equitable shares of the provinces. This could result in a decreased amount being transferred to the Provincial Exchequer Account.

Provincial departments own revenue may not reach the budgeted amount, or may experience dips in anticipated revenue flows, which will reduce the flow of income to the Provincial Revenue Fund. If a provincial department does not realise its budgeted revenue for a specific financial year, the expenditure levels must be reduced accordingly.

The financial institution with which investments are placed may for many reasons not be in a position to repay the capital and interest upon maturity.

The national Treasury has recently proposed that the equitable share and conditional grants earmarked for this Province should, be credited directly to an account held at the Corporation for Public Deposits. This mechanism has, however, not been finalised but if implemented, there is a real risk that the interest earnings will be substantially less than is currently generated and that the interest projections in terms of the Medium-Term Expenditure Framework will not be realised.

An initiative launched by the national Treasury that questions large provincial bank and cash balances has recently been presented to provinces for discussion. Apart from running counter to the principles underpinning financial asset management, assessing accumulated capital cannot be done on a simplistic cash basis, but requires taking aboard accumulated liabilities or commitments, inclusive of specific economic infrastructure investment initiatives. Therefore balances at face value cannot be regarded as an unfettered cash reserve. In any case, if balances were to be artificially reduced, the risk of an overdraft situation is a real possibility.

Liabilities versus cash

Cash reserve

The increasing demands being made on the Social Services budget in the Province will most likely result in overspending by this department for the current and ensuing financial years. Further pressures are building up at Education and Health, requiring rather innovative steps apart from adjustment, particularly for Social Security, of the vertical share distribution of nationally received revenues between the three spheres of government. If additional resources cannot be found and directed to these sectors, the continued provision of services of an acceptable standard might be jeopardised. If such moneys do not materialise, funding will have to be obtained by restructuring the Province's own resources to finance any shortfalls.

Currently, the Provincial Revenue Fund has a net uncommitted cash reserve of about R33 million, which represents the beginning of the second cash transfer to the Department of Transport and Public Works for agreed to infrastructure investment in synergy with other economic development initiatives currently under consideration.

Smoothing

To compensate for the variability in internal revenue flows, it was necessary to smooth the Province's current and capital outlays with total revenue received over the 2002/03 – 2004/05 MTEF period to ensure that expenditure is kept relatively constant in real terms for all departments. The current smoothing was financed from anticipated revenue receipts over the full MTEF term, but work is underway to find a more efficient method. One possibility is to put the outstanding cheque list to better use. Smoothing in this manner should not have a negative impact on cash flow as the outstanding cheque list, amounting on average to R30 million after allowing for electronic funds transfers (EFT's), should allow the availability of funds on a rolling basis. The gap between orders placed and payment on delivery allows a further cushion.

Conclusion

The main intention is to ensure that cash flow management in the Province is maintained at its current high levels of efficiency and to keep on striving for improvement in all the spheres related thereto. The positive spin-off of these practices will be to place investments at various financial institutions according to an approved investment policy, which will result in the receipt of optimum interest gains. This in effect will mean that interest will be constantly capitalised, resulting in the accumulation of capital, which will in turn be utilised to finance major infrastructure projects. In maintaining minimal cash and bank balances, the risk of an overdrawn position is ever present and will require innovative steps to remain cash positive.

4.7 Accounting

Overview

With the inception of the Interim Constitution in 1994, the need to reorganise and rationalise government departments was identified as a priority, *inter alia* to improve service delivery in government departments, which functioned in terms of the old Exchequer Act (Act 66 of 1975) and Treasury Instructions. During this process, improving financial management in departments was also identified as a long-term goal. This, *inter alia*, entailed the decentralisation of the Departmental Accountant Services to provincial departments and the establishment of the provincial Treasury to control financial management in departments. To address the limited capacity within provincial departments at the time and as a forerunner to the decentralisation of the Departmental Accountant Services, financial expertise from the Departmental Accountant was placed within the various provincial departments as Financial Management Representatives. These Representatives had extensive financial management experience and proved to be successful.

The readjustment of the functions of the heads of provincial administrations and provincial departments in accordance with the Public Service Laws Amendment Act, effected in 1999, and in keeping with the spirit of the Public Finance Management Act, 1999, (PFMA) the provincial Treasury continued the process of decentralising the Departmental Accountant Services, which operated on the centralised Financial Management System (Department 70), to the respective departments. This was a phased approach, with the first phase taking place during the 1999/2000 financial year, the second phase during the 2000/2001 financial year and the third and final phase during the 2001/2002 financial year. Hence, the discontinuation of the centralised Departmental Accounting Services with effect from 1 April 2002. Each department now operates as a separate department on the Financial Management System and can be held accountable for its actions.

The enactment of the PFMA in April 2000 also necessitated the establishment of a provincial Accountant-General component within the provincial Treasury, whose main purpose is to ensure that norms and standards within the legislative framework are implemented and complied with in provincial departments. An evaluation by the Norms and Standards component in the provincial Treasury on the implementation of the PFMA for the period post-2000 revealed a 90% success rate in provincial departments. It should, however, be noted that the evaluation was based on nominal compliance with the PFMA and focused mainly on the seven immediate priorities mentioned in the Accounting Officers Guide, viz. in-year management, monitoring and reporting; clearing up audit queries; establishing effective internal controls; improving expenditure management and transfers; establishing a framework for banking arrangements; completing the financial statements on time, and the delegation of responsibilities. It is pleasing to note that the financial statements in the new format (GRAP) were submitted to the Auditor-General within the prescribed timeframes by all departments for the two years running.

Internal prescripts, viz. Provincial Treasury Directives, were developed for the Province as an interim measure. These have been revisited and were reissued with effect from 1 December 2001 as Provincial Treasury Instructions. This allowed for the effective transition from the old to the new prescripts. Guidance was also given to departments on the issuing of departmental internal financial prescripts not inconsistent with the prescribed norms and standards. The provincial Treasury is in the process of revising the existing Provincial Treasury Instructions, which will be in line with the new Treasury Regulations issued on 27 May 2002.

Accounting policies and related matters

The financial statements are prepared in accordance with the following policies, which are applied consistently in all material respects. However, where appropriate and meaningful, additional information is disclosed to enhance the usefulness of the financial statements and to comply with the statutory requirements of the Public Finance Management Act, Act 1 of 1999 (as amended by Act 29 of 1999), the Treasury Regulations for Departments and Constitutional Institutions issued in terms of the Act, and the Division of Revenue Act, Act 1 of 2001.

- Basis of preparation

  The financial statements are currently prepared on the cash basis of accounting except where stated otherwise. Under the cash basis of accounting, transactions and other events are recognised when cash is received or paid. This basis of accounting measures financial results for a period as the difference between cash receipts and cash payments. The basis of preparation will, however, evolve as we progress towards accrual based accounting.

- Revenue

  Voted funds are the amounts appropriated to a department in accordance with the final budget (original plus the adjustment estimate). Interest received is recognised upon receipt of the funds, and no accrual is made for interest receivable from the last receipt date to the end of the reporting period. Unexpended voted funds are surrendered to the Provincial Revenue Fund.

  Dividends received are recognised as revenue in the financial statements of the department, however, it is also recognised as an expense in the same year, as the dividends are paid over to the Provincial Revenue Fund.

- Expenditure

  Capital and current expenditure is recognised in the income statement when the payment is made. Interest paid is also recognised when paid and no accrual for interest is made between the payment date and the reporting date.

- Unauthorised, irregular, and fruitless and wasteful expenditure

  Unauthorised expenditure means the overspending of a vote or a main division within a vote, or expenditure that was not made in accordance with the purpose of a vote or, in the case of a main division, not in accordance with the purpose of the main division. Unauthorised expenditure is treated as a current asset in the balance sheet until such expenditure is recovered from a third party, authorised by the provincial Parliament, or funded from future voted funds.

  Irregular expenditure means expenditure, other than unauthorised expenditure, incurred in contravention of or not in accordance with a requirement of any applicable legislation, including the Public Finance Management Act, the State Tender Board Act, or any regulations in terms of this Act, or any provincial legislation providing for procurement procedures in that provincial government . Irregular expenditure is treated as expenditure in the income statement until such expenditure is either not condoned by provincial Treasury or the Western Cape Provincial Tender Board, at which point it is treated as a current asset until it is recovered from a third party.

  Fruitless and wasteful expenditure means expenditure that was made in vain and would have been avoided had reasonable care been exercised. Fruitless and wasteful expenditure is treated as a current asset in the balance sheet until such expenditure is recovered from a third party.

- Debts written off

  Debts are written off when identified as irrecoverable. No provision is made for irrecoverable amounts.

- Assets

  Physical assets (fixed assets, movable assets and inventories) below R5 000 are written off in full when they are paid for and are accounted for as expenditure in the income statement. Physical assets above R5 000 are capitalised and are accounted for in the balance sheet. Depreciation on capitalised assets is accounted for in the income statement.

  Receivables

Receivables are not normally recognised under the cash basis of accounting. However, receivables included in the balance sheet arise from cash payments that are recoverable from another party.

- Payables

Payables are not normally recognised under the cash basis of accounting. However, payables included in the balance sheet arise from cash receipts that are due to either the Provincial Revenue Fund or another party.

- Provisions

Provisions are not normally recognised under the cash basis of accounting.

- Lease commitments

Lease commitments for the period remaining from the accounting date until the end of the lease contract are disclosed as a note to the financial statements. These commitments are not recognised in the balance sheet as a liability or as expenditure in the income statement as the financial statements are prepared on the cash basis of accounting.

- Subsequent payments

Payments made after the accounting date that relates to goods and services received before or on the accounting date are disclosed as a note to the financial statements. These payments are not recognised in balance sheet as a liability or as expenditure in the income statement as the financial statements are prepared on the cash basis of accounting.

- Employee benefits

Short-term employee benefits

The cost of short-term employee benefits is expensed in the income statement in the reporting period that the payment is made. Short-term employee benefits that give rise to a present legal or constructive obligation are deferred until they can be reliably measured and then expensed. Details of these benefits and the potential liabilities are disclosed as a note to the financial statements and are not recognised in the income statement.

Termination benefits

Termination benefits are recognised and expensed only when payment is made.

Retirement benefits

The department provides retirement benefits for its employees through a defined benefit plan for government employees. These benefits are funded by both employer and employee contributions. Employer contributions to the fund are expensed when money is paid to the fund. No provision is made for retirement benefits in the financial statements of the department. Any potential liabilities are disclosed in the financial statements of the Provincial Revenue Fund and not in the financial statements of the employer department.

Medical benefits

The department provides medical benefits for (certain/all) its employees through defined benefit plans. These benefits are funded by employer and/or employee contributions. Employer contributions to the fund are expensed when money is paid to the fund. No provision is made for medical benefits in the financial statements of the department.

Retirement medical benefits for retired members are expensed when the payment is made to the fund.

- Capitalisation reserve

  The capitalisation reserve represents an amount equal to the value of the investments and/or loans capitalised, or deposits paid on behalf of employees of a foreign mission, for the first time in the previous financial year. On disposal, repayment or recovery, such amounts are transferable to the Provincial Revenue Fund.

- Recoverable revenue

  Recoverable revenue represents payments made and recognised in the income statement as an expense in previous years, which have now become recoverable from a debtor due to non-performance in accordance with an agreement. Repayments are transferred to the Provincial Revenue Fund as and when the repayment is received.

- Comparative figures

  Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year. The comparative figures shown in these financial statements are limited to the figures shown in the previous year's audited financial statements and such other comparative figures as the department may reasonably have available for reporting.

General concerns with accounts in the Province

- Establishing the net effect of assets and liabilities in the Province

  There is genuine concern to establish the net effect of assets and liabilities in the Province in order to be in a position to commit unattached reserves. In the light of possible hidden liabilities in the books of accounts emanating from the rationalisation process in respect of the tricameral system and the former Cape Provincial Administration, this aspect was taken up under Statement of Contingent Liabilities in section 4.8.1.

- Qualified Auditor-General reports

  The trend regarding the qualification of audit reports for the 1998/1999 and 1999/2000 financial years reflected a decrease from 47% to 28%. However, qualification of the audit reports for the 2000/2001 and 2001/2002 financial years reflected a marginal increase to 30%. The qualification of audit reports in general is largely due to the lack of capacity in departments. The key areas of audit qualification are poor internal checking and control, and asset management.

- Internal audit/Audit Committee

  Notwithstanding this Province having a shared Audit Committee and a centralised Internal Audit unit, the reliability of these units, which is an important tool for proper fiscal discipline, appears to be of concern. The Auditor-General, in his audit report for the 2000/01 financial year, could rely on the work of the Internal Audit unit only to a limited extent. Capacity constraints were cited as the primary factor that hampered the work of Internal Audit. Although the Auditor-General's opinion for the 2001/02 financial year progressed to moderate reliance on the work of the Internal Audit unit, full reliance should be the ultimate goal pursued by the Internal Audit unit.

  Some of the benefits of internal audits are:

  - ♦ Internal Audit reviews operations and programmes to evaluate whether (a) goals and objectives which are consistent with those of the organisation have been established, (b) adequate performance criteria have been established to measure accomplishment, (c) goals and objectives are being met, (d) the manner in which goals and objectives are met is consistent with organisational values, and (e) accountability has been established.

  - ♦ It also carries out risk assessment pertaining to the information systems environment, the reliability and integrity of financial and operational information, the effectiveness and efficiency of operations, the safeguarding of assets and compliance with laws, regulations and contracts and must be conducted at least annually. Based on the results of the risk assessment, internal audit should evaluate the organisation's controls to determine their effectiveness and efficiency and make recommendations aimed at improving them.

- Limited interpretative skills, coupled with the lack of understanding of the financial reforms required of the PFMA.

  Departments have shown limited knowledge with regard to analysing accounting reports, financial statements, etc. with a view to taking timeous corrective actions to remedy identified shortcomings. This could lead to poor financial management, including an unhealthy state of the books of account, which, in turn, could result in poor financial statements and qualified audit reports. In addition, departments have shown a tendency to comply only nominally with the requirements of the PFMA instead of invoking the financial reforms intended by the PFMA. The following are areas of concern where departments have complied only nominally with the PFMA without adding value to the standard of service delivery, performance and effective financial management:

  - Macro risk assessments have been carried out in departments instead of detailed risk analyses;
  - Resultant strategies, viz. fraud prevention plans, are largely ineffective to manage risks due to macro assessment;
  - Analysis of audit reports has been poor, if done properly, such analysis would prevent repetition of shortcomings.

- Replacement or upgrading of financial systems

  Having highlighted the above concerns, it is also important to highlight the inadequacies of the financial administration systems as a concern. The existing financial administration systems need to be upgraded if departments, including the provincial Treasury, are to reap the full benefits intended by the PFMA and to enable accounting officers to discharge their financial management obligations properly, as required by the PFMA. Slow progress in this regard hampers the full implementation of GRAP, especially with the intended shift from a cash to accrual basis of accounting, and the facilitation of proper performance management by accounting officers. Progress in this regard is therefore also of paramount importance. The national Treasury has identified the Integrated Finance Management Solution as the system to resolve these shortcomings. For more details, see section 4.4.

Way forward

- The provincial Treasury needs to prioritise and champion the implementation of the PFMA and ensure that the implementation is in line with the objectives and the spirit of the PFMA. In order to improve fiscal discipline in the Province, it is essential that the provincial Treasury should enforce the national and provincial norms and standards in provincial departments and ensure the proper functioning of intergovernmental systems, internal controls, risk management processes and the accountability chain.

- Mooting the idea of a separate Audit Committee and Internal Audit units by the provincial Treasury can be seen as the first steps towards improving the effectiveness and reliability of these units by the Auditor-General. The first phase involves the decentralisation of the shared Audit Committee during the 2002/03 financial year, followed by the decentralisation of the centralised Internal Audit unit during the 2003/04 financial year as the second phase. The Western Cape Cabinet approved on 14 August 2002 that three different Audit Committees be established in the Western Cape Provincial Administration. The decentralisation was based on the 80/20 principle, which in effect will mean that the bigger departments, viz. Education and Health and possibly Social Services and Poverty Alleviation will have their own Audit Committee and Internal Audit units. The remaining departments will have a shared Audit Committee and a centralised Internal Audit unit. If necessary, the future position of the shared Audit Committee and centralised Internal Audit units for the remaining departments will be reviewed for the purpose of maintaining their effectiveness.

  There is considerable value in investing in Internal Audit. Thus it is essential that accounting officers should allocate adequate funds to ensure effective Internal Audit units.

- Although it is essential that departments should comply at least nominally with the relevant prescripts (regulatory framework, reporting requirements and timelines) it is also important that the financial practitioners should start grappling with substantive implementation of the PFMA, which will entail the ability to set benchmarks (quality) for financial management and financial functionaries (CFO structure) standards. Central to the success of this is capacity building.

- The process of setting standards of generally recognised accounting practice and of publishing directives and guidelines concerning the standards should be prioritised and expedited by the Accounting Standards Board. Although we are aware that the Accounting Standards Board is in its early stages of operation, the following are priority areas that the Board needs to focus on:

  - The Chart of Accounts that will ensure transparency in government accounting,
  - GRAP standards for financial statements;
  - Standards for asset management, in particular asset valuation and depreciation.

  This will enhance accountability by producing quality financial statements coupled with appropriate interpretative and analytical accounting skills in departments, public entities and treasuries as accrual-based accounting evolves.

- In terms of sections 6(2)(c) and 18(2)(d) of the PFMA, the relevant Treasury is required to monitor and assess the implementation of national and provincial norms and standards in public entities. In order to assist the designated department in playing an effective oversight role in respect of public entities, a “PFMA checklist for public entities” was developed and implemented. This should be seen as the first step towards promoting public entity compliance with the basic requirements of the PFMA, in other words, nominal compliance. Based on the progress reports received for the first quarter of 2002, the following key focus areas have been complied with by public entities:
  - Processes have been established to oversee public entities (section 63(2) of the PFMA);
  - Public entities have submitted quarterly reports to executive authorities (TR 26.1.1);
  - All public entities have submitted their strategic plans for the 2002/03 financial year to the relevant executive authority for approval;
  - Written assurances in terms of section 38(1)(j) have been obtained;
  - All public entities have submitted their financial statements for the 2001/02 financial year to the Auditors and the provincial Treasury in terms of section 55(1)(c).

- As we progress towards accrual-based accounting, recording and reporting of assets in the books of account is increasingly becoming a priority. In order to facilitate the process, national Treasury has suggested the following:

  Assets acquired from 1 April 2002 should be capitalised and reflected on the financial statements for 2002/03. The recording of existing assets by all the departments should be completed by:

    - December 2002 for assets bought in 2001/2002
    - March 2003 for assets bought in 2000/2001
    - September 2003 for assets bought in 1999/2000
    - March 2004 for assets bought prior to 1999/2000

Assets valued at R5 000 and above are to be capitalised and depreciated over its useful life (major asset), and assets valued below R5 000, expensed and classified on the assets register as controlled assets (minor asset). The classification of asset categories (for disclosure in financial statements and recording in fixed asset register) is adopted from the various accounting standards, International Federation for Accountants (IFAC), Accounting Standards Board (ASB) and Government Financial Statistics (GFS). A straight-line depreciation method is used for all asset categories in the departments. Depreciation is an instrument used to recognise the cost of consuming the service potential of an asset over time and provides a means of accounting for the cost of an asset over its useful life.