

Country Paper

The Supreme Audit Institution (SAI) of South Africa's approach to supporting financial audits on human resources, payroll and supply chain management through the use of data analytics.

23 May 2017



CAATs approach to support financial audits on human resources, payroll and supply chain management

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1. Information systems auditing

In order to keep up to date with the government transition from manual processing to automated processing, the Auditor-General of South Africa (AGSA) started conducting information technology (IT) audits in the early 1990s. A specialised Information Systems Auditing (ISA) business unit was established to provide support to all business units of the AGSA.

ISA forms an integral part of the audit processes of the AGSA and supports various financial audit business units (ABUs) by evaluating IT internal controls as part of the AGSA's integrated audit approach. ISA assists ABUs in efficiently and effectively discharging their responsibilities in the IT environment where financial and performance information is generated. ISA also supports the Investigations Business Unit (IBU) by conducting ongoing data analytics of the public entities' payment systems using computer-assisted audit techniques (CAATs) to identify and verify possible red flags.

ISA performs IT audits for two cycles, i.e. the Public Finance Management Act (PFMA) cycle, which includes the national and provincial departments and public entities, and the Municipal Financial Management Act (MFMA) cycle, which included municipalities and municipal entities, in an audit year. For both audit cycles, complete IT audits are performed by ISA on transversal systems and complex systems, which range from Enterprise Resource Planning (ERP) to single/multi-purpose standalone systems at the following types of auditees:

- National departments
- Provincial departments
- Public entities
- Metropolitan municipalities
- Municipalities and municipal entities utilising complex systems.

For less matured IT environments, high-level audit checklists are performed by the regularity auditors. Regularity auditors are responsible for examining local, provincial and national government's use of public funds and providing an independent opinion on their financial statements and performance against predetermined objectives.

1.1. What is information systems auditing?

Information systems (IS) auditing is the examination of the controls within an entity's IT environment. It focuses on determining whether adequate controls that are operating effectively are in place to mitigate risks to ensure that data is protected, reliable and available.



Types of audits we perform

IS audit support can be categorised as follows:

- **Auditing of IT general controls** - Controls that are present in the environment surrounding the application systems. These controls include the organisational and administrative structures of the IT function, the policies and procedures in place, security management, change control, data backups and recovery, as well as infrastructure and environmental controls.
- **Auditing of application controls** – Controls that are present within the application systems. These controls include validation of data input, adherence to business rules, and logical access to the application systems, exception handling and event logging.
- **Data analytics** - The process of collecting, organising and analysing large sets of data to discover patterns and other useful information.
- **Project risk assurance** – Assessment of the controls within the development or implementation of application systems in order to provide insightful, independent and informed recommendations to auditees and so-doing reduce the risk of project failure and increase business value. start
- **Enterprise resource planning system assurance** – Assessment of the controls within ERP systems, e.g. the Systems, Applications and Products System (SAP), JD Edwards System (JDE) and Oracle.
- **Network security** – Assessment of the security of the system's physical configuration and environment, software, information handling processes, and user practices. Assessments typically include firewall reviews, database and vulnerability assessments.
- **IT research and development** – Researching and updating IT audit methodologies in line with current standards, guidelines and trends and in support of the AGSA's integrated auditing approach.
- **Product champion** – A centre responsible for the general reports and quality reviews. General reports are the outcome of the audits conducted by the AGSA at all the South African municipalities, municipal entities, national, provincial government departments and state-owned enterprises across the nine provinces. The information and insights presented in this flagship publication are aimed at empowering oversight structures and executive leaders to focus on those issues that will result in reliable financial statements, credible reporting on service delivery and compliance with key legislation. The centre is also responsible for providing assurance to the ISA leadership on the operating effectiveness of the system of quality control within the



AGSA to facilitate the adequacy and efficiency of all AGSA processes, which in turn contributes to a high standard of staff competence, work ethic and quality of reporting.

1.2. Structure of ISA

The ISA staff complement comprises of 167 employees. The unit is headed by the business executive, supported by two deputy business executives and 14 senior managers. The majority of the staff members hold post-graduate degrees and 80 are certified information systems auditor (CISA). The following is a high-level overview of ISA at glance:



1.3. Contract work

Due to the large volumes of audits to be conducted by ISA (approximately 810 audits), some are outsourced to audit firms in order to meet the audit coverage. Audits are either contracted in or contracted out.

Contracted-in work: Supply of various levels of staff by the private audit firm to work under the supervision of the AGSA audit management. However, the private audit firm management would still be responsible for the development and expected quality output of the staff members.

Contracted-out work: Allocation to the private audit firm of full responsibility up to draft audit report stage for the performance of an audit.

1.4. Evolution of IT audit in South Africa and milestones achieved

Some of the milestones achieved to date include the AGSA's involvement in the assessment of the shortcomings in IT alignment to service delivery with the outcomes of the assessment being currently implemented by relevant role players in the IT landscape of government. The AGSA is also involved as an external assurance provider on the implementation of the Integrated Financial Management System (IFMS) which aims to replace the transversal systems that are currently in use at departments. Furthermore, the Department of Public Service Administration has developed an IT governance framework in response to recommendations made by the AGSA.

The purpose of the framework is to promote uniformity in the governance of IT in the public sector and ensure integration of governance of IT into the department corporate governance structures and processes, which will build the foundation for the implementation of IT processes.

1.5. Innovative ideas/techniques for IT audit

The roll-out of the National Development Plan (NDP) and the planned implementation of IFMS, inter alia, are indications of the changes in the governmental environment of South Africa. These changes are some of the aspects affecting auditing and in particular IT auditing in the public sector in South Africa. As such, the AGSA recognised the need to realign itself and its strategic view of South Africa to audit what matters. This came about through the development and approval of the new 2024 strategy of the AGSA, commonly known as the "4 V strategy" which focuses on the aspirations that the AGSA has for South Africa (refer to figure 1) and the approach of "getting there" (refer to figure 2).

Figure 1- AGSA's aspiration (Source: AGSA strategic plan)



We aspire to see a public service that is characterised by the following:

1. Strong financial and performance management systems

- Transparent and stable financial and performance management
- Reporting systems
- Budgeting and planning processes that ensure the effective, efficient and economical use of all public resources
- Strong internal audit capabilities that provide assurance.

2. Commitment and ethical behaviour by all

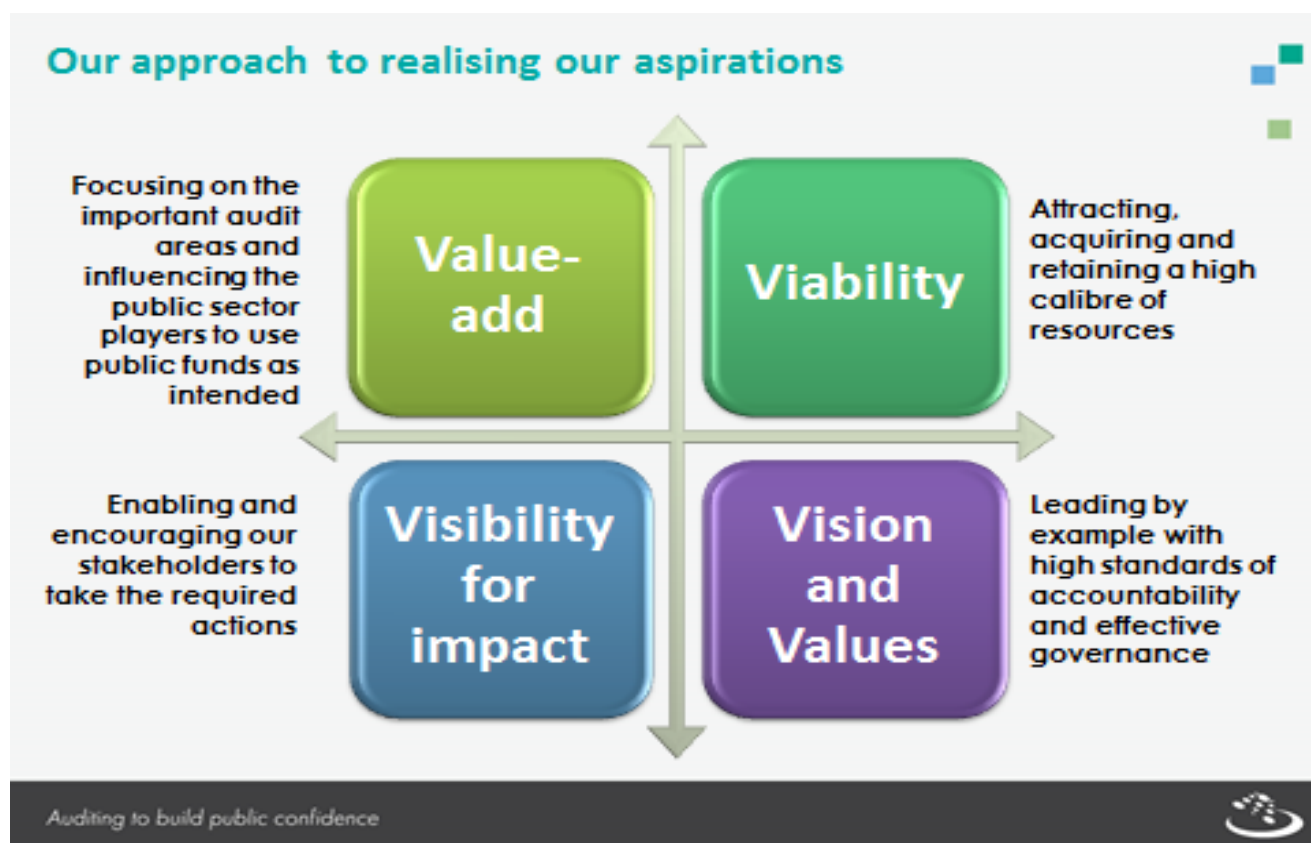
- Visible commitment by all players in the public service to contribute towards the financial health of the country and an improved social reality for our people
- Demonstrated ethical behaviour and professionalism in the public sector as cementing characteristics of a capable state, with a public service that consistently does the right thing.

3. Oversight and accountability

- Accurate and empowering financial and performance reporting to enable effective oversight

- An appreciation of the role of applying consequences for transgressions and poor performance in restoring the integrity of, and building public confidence in, the system of public administration.

Figure 2: Approach to realising aspirations (Source: AGSA strategic plan)



Our commitments for the period 2017 - 20 are structured around four strategic goals:

1. Value-adding auditing

- This is aimed at providing audit-derived valuable insights to our stakeholders on the status of their internal control and performance environment accompanied by actionable recommendations, which – if executed – would lead to visible improvements in public sector administration.

2. Viability

- This internally focused perspective of our work ensures that we have the necessary resources: an enabling legal framework, independent financial resources, and the required skills, competencies and culture to execute our mandate economically, efficiently and effectively.

3. Visibility

- This internally focused perspective of our work ensures that we have the necessary resources: an enabling legal framework, independent financial resources, and the required skills, competencies and culture to execute our mandate economically, efficiently and effectively.

4. Vision and values

- Through our work and behaviour, we aim to lead by example and to continually demonstrate that clean administration is achievable.

ISA's role in realising these aspirations was to contribute towards developing strategic projects focused on the following:

- **Data analytics**, to improve our audits and the value it can add by making more efficient and effective use of the data
- **Intensified integration within the organisation** – having the right combination of skills and competence within the audit teams
- Having an **in-depth understanding** of the auditee environments
- Doing things **quicker and smarter**.

In support of the above efforts to improve the overall audit process, the AGSA developed an integration plan which aims to have audit areas such as Regularity Audit, Performance Auditing, Investigations, ISA and Audit Research and Development (ARD) pulling together into one team in order to achieve audit efficiencies and add value for auditees.

The AGSA also embarked on a project to enhance audits through the use of data analytics in support of Vision 2024 (improving the lives of citizens) which is largely dependent on ISA's ability to raise the level of use of data analytics from its current state, where only ISA performs data analytics, to the desired state of empowering all regularity auditors throughout the organisation to perform basic analytics without specialist supervision to ultimately achieve the end state of using data analytics to drive audits and not only to enhance them.

2. Data analytics

ISA, as the leading provider and developer of data analytics in the audit environment of the organisation, has been tasked to define the implementation approach to realise the AGSA's strategic vision of developing and embedding data analytics in the audit process. ISA has laid out a tangible



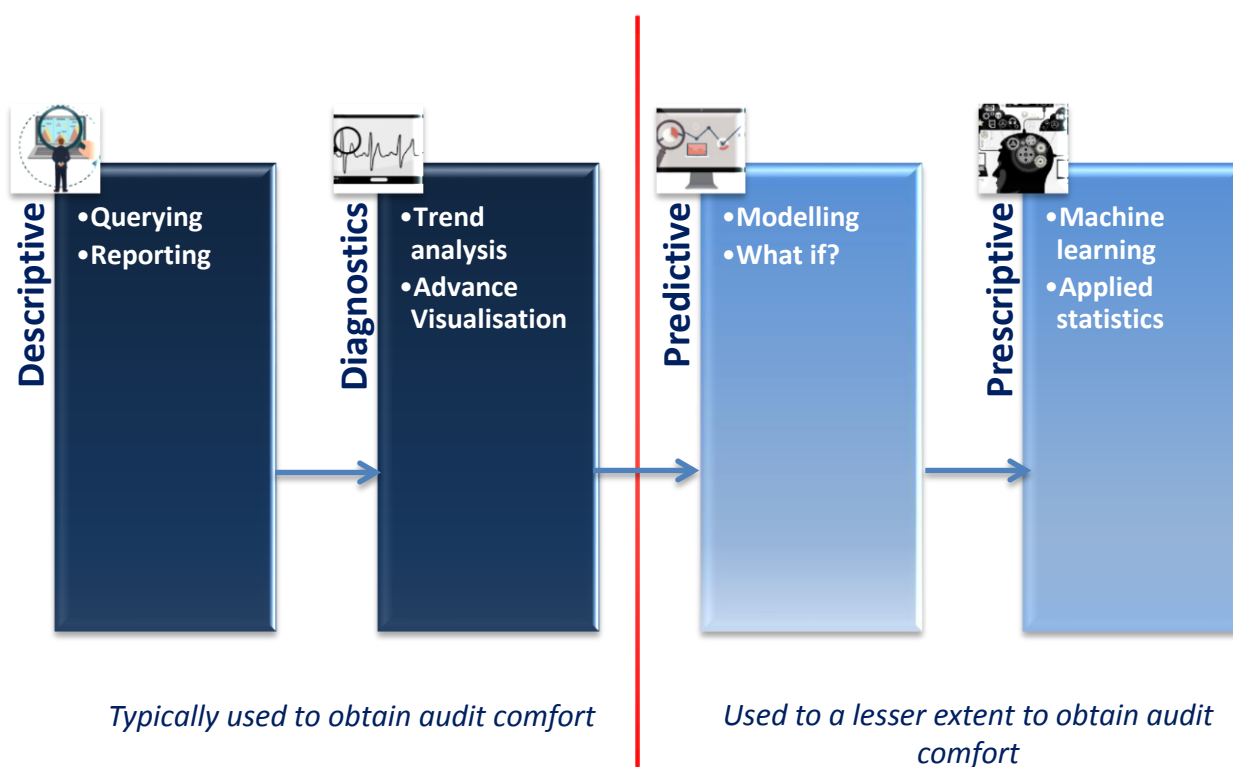
approach to achieving the AGSA's vision. In doing so, ISA consulted with relevant stakeholders to develop a collective approach that meets the needs of their key stakeholder, namely Regularity Audit.

The objectives of the AGSA's data analytics strategy are defined as follows:

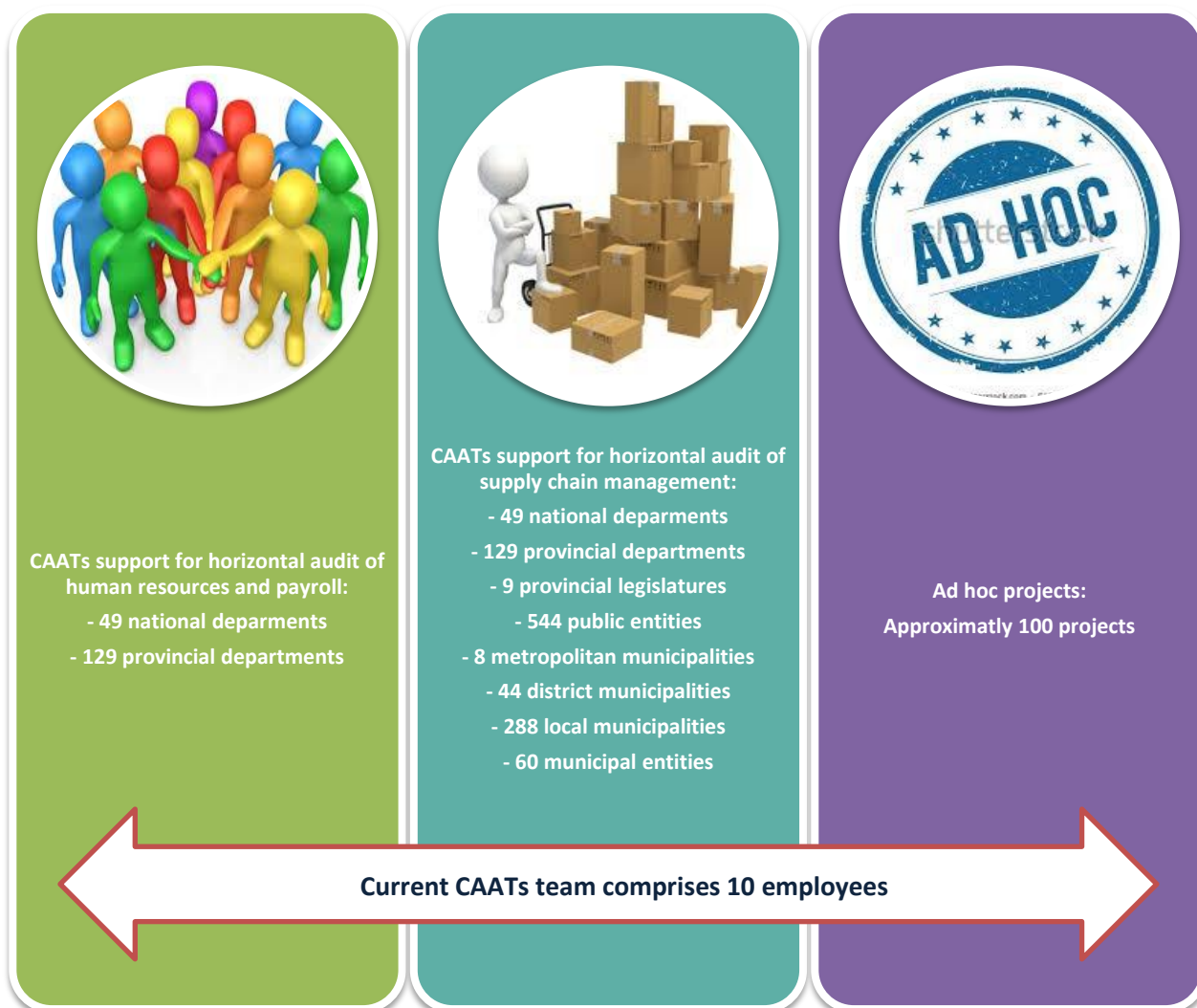
- **Audit what is relevant** – focus on risks; audit full populations of data to obtain better audit coverage; use insights gained from data to focus the audit approach and improve audit planning.
- **Audit in a more efficient manner** – deliver a better-quality audit using the same resources; reduce the time it takes to complete audit steps without compromising quality and audit coverage.
- **Reduce the audit risk** – reduce the probability of failure to detect material misstatements which could lead to an incorrect audit opinion.
- **Add more value to our auditees** – deliver more than just a financial audit; focus on the business risks of our auditees and the sustainability of their organisations.

2.1. What is data analytics?

Data analytics means different things to different institutions. In the context of auditing, descriptive and diagnostic data analytics is primarily used. In the AGSA the main purpose of data analytics is to support the regularity auditors, either during the planning or the execution phase of an audit. It mainly comprises the following areas:



This is typically performed under the banner of CAATs, using advanced data querying techniques to process large volumes of data. Trend analysis tools and data visualisation techniques are also used to identify areas of high risk and anomalies to improve audit planning and enhance the ability to focus our audit effort on what matters. The data analysis team is currently responsible for the following:



Due to the extent of work to be performed by the CAATs team, an automated solution was developed, including the following:

- CAATs support for horizontal audit of human resources and payroll
- CAATs support for horizontal audit of supply chain management.

3. Horizontal auditing

Horizontal auditing is a process whereby a single business unit or team performs audit processes and procedures that are common to a number of engagements with a predetermined focus.

The objectives of performing a horizontal audit are typically to:

- increase audit efficiency – decreasing the audit time while still meeting professional standards
- improve the quality of audit procedures
- improve consistency between engagements, which promotes consistent reporting.

The horizontal audit process is currently used in the audit of human resources and payroll, as well as procurement and contract management.

3.1. Horizontal audit approach

A horizontal audit approach is determined with reference to the viability of performing audit processes and procedures centrally. This, in turn, is driven by factors such as:

- commonalities in the environments of the auditees, e.g. same sphere of government or sector within government and shared/similar objectives and strategies, governance structures, accounting policies, etc.
- the availability of central, standardised data
- the same or similar information systems and business processes at the auditees
- the nature of transactions that favours routine transactions
- whether the environments are adequately regulated to enable the central development and execution of audit procedures.

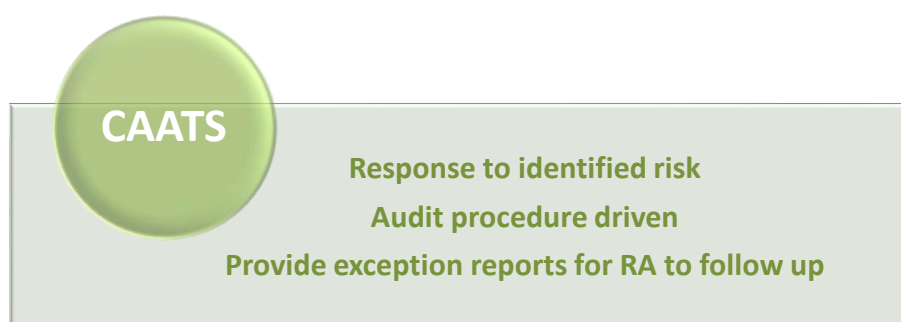
The advantages of the approach are illustrated as follows:



- Improve efficiencies by following the horizontal approach – less time is spent on the employee cost component
- ARD develops the CAATs working papers and audit procedures to be performed centrally. This enables consistency in execution and reporting, while the quality of audit procedures performed is ensured
- Centrally available data ensures ease of data access and horizontal testing.

3.2. Computer-assisted audit techniques

The AGSA is using CAATs more often as part of the audit process and to support substantive audit procedures.

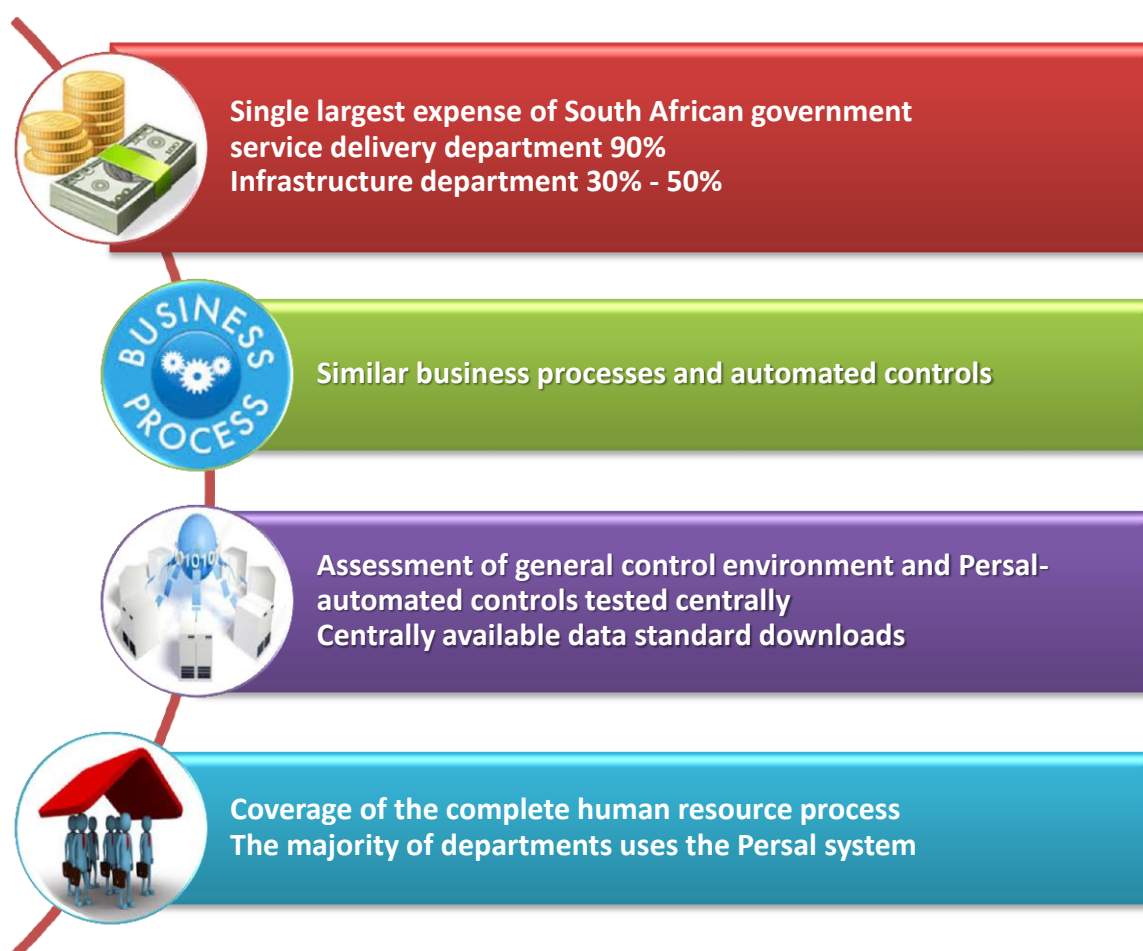


Data is being downloaded from various systems and used as basis for attaining/reaching an opinion on financial statement accounts. Currently CAATs is a tool available to each and every auditor to be applied at their discretion during an audit.

Due to the large volume of transactions in the government environment and in view of the complicated nature of information systems, it has become essential to make use of CAATs in audits. CAATs are computer programs used by the auditor to perform certain audit procedures, such as sampling, testing for duplicate transactions, testing of the accuracy of transactions, summarising of information according to certain criteria, etc. CAATs therefore improve the effectiveness and efficiency of audit procedures, especially where population sizes are very large.

4. Human resources and payroll analytics

The following factors were considered for the horizontal approach:



4.1. Approach followed

The following are key factors which were taken into account to determine the approach:



INPUT

- Employee master data (monthly basis) approx. 1,5 million
- Transaction data (monthly basis) approx. 40 million transactions
- Overtime data (monthly basis)



Processing/converting (ACL)

- 166 national and provincial departments and entities
- Automated solution
- Standardised data sets
- CAATs are designed and tested by ARD

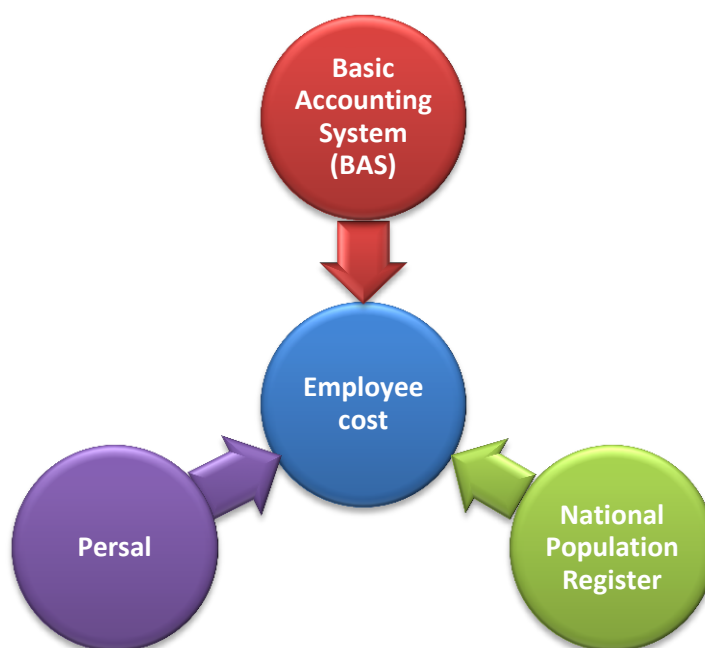


Output

- 29 programmatically generated working papers per entity
- 62 standard tests and indicators included in the working papers
- R&D-developed procedures and working papers
- Entire population tested for specific risk areas

Input

Persal is a standard system that was developed in-house by National Treasury and is currently centrally controlled and maintained by the State Information Technology Agency (SITA) but owned by the National Treasury. Persal is used by national and provincial government departments to manage their financial affairs with regards to employees.



- BAS data is used for reconciliation purposes to establish completeness and accuracy of the Persal data.
- The National Population Register is used to determine valid identification numbers and deceased employees
- Persal data is therefore the main source for the tests performed and working papers generated.

The data indicated below is downloaded by SITA on the basis of a feasibility study conducted by the AGSA and is collected on a monthly basis as dictated by month closure dates.

- Salary transactions data: monthly
- Overtime data: monthly
- Management information system (master data): monthly

Government established various departments to assist in reaching its objectives. Government-established institutions are registered on the Persal database as users. These comprise **169** national and provincial departments which are the focus of the horizontal CAATs on employee cost.

The breakdown of the departments (national and provincial) is as follows:

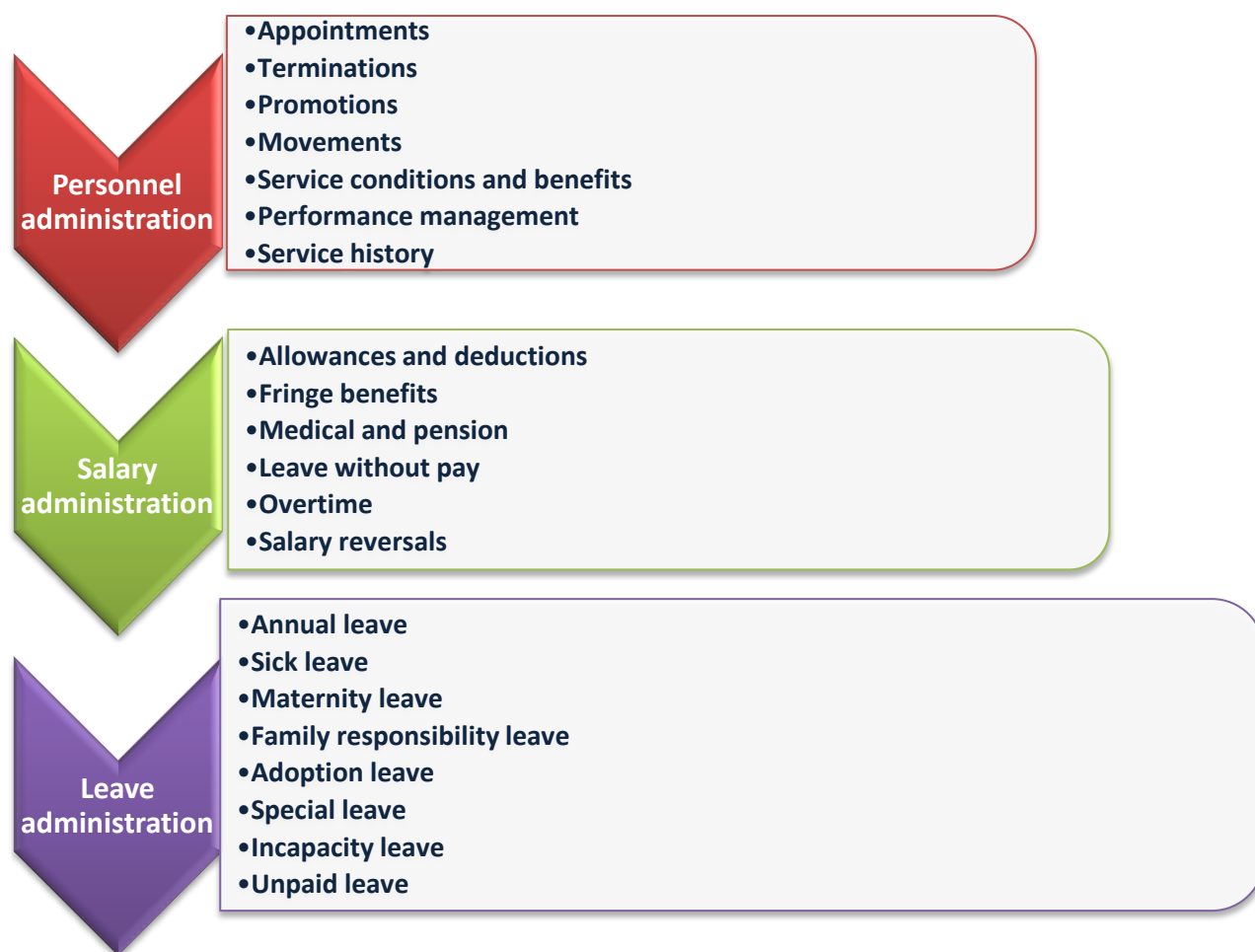
- 48 national departments
- 14 Eastern Cape provincial departments
- 12 Free State provincial departments

- 14 Gauteng provincial departments
- 15 KwaZulu-Natal provincial departments
- 13 Limpopo provincial departments
- 12 Mpumalanga provincial departments
- 13 Northern Cape provincial departments
- 13 North West provincial departments
- 14 Western Cape provincial departments.

Persal is an integrated public service (human resources) with over 25 000 users who access the system via linked main frames across South Africa. Approximately 40 million transactions are processed each year and approximately 1,5 million government employees are paid via the system each month.

The system was designed and written to cater for all aspects of government regulations, prescripts, treasury regulations and policies. All the national and provincial government departments use the Persal system. It runs on five bureaux with six production environments. The system has been in a production environment since 1990, but is constantly adapted to keep pace with changes in technology and policy, and efficiently addresses the user requirements by virtue of a suite of professional procedures as described in the ISO9001 Standards.

The Persal system has the following main areas of management:



Processing

The purpose is to render assistance to the regularity auditors responsible for the auditing of the financial statements of the various national and provincial government departments (auditees) by means of monthly conversions of data downloaded from Persal. The converted data is needed by the regularity auditors during the analysis and substantiation of transactions generated by Persal. Audit Command Language (ACL) software, which is used to convert the data into a process-able format.

Output

The detail transaction data will form the basis of CAATs, while the CAATs to be performed will be executed against the reconciled data. The Persal reconciliation working paper serves as evidence of the completeness of the data and that the data has been reconciled with the trial balance on a monthly and year-to-date basis. This will ensure the validity and accuracy of the exception reports and samples generated. ACL will be used for executing the CAATs and the results will be generated and made available for further testing and follow-up by regularity auditors. Furthermore, the Persal CAATs manual



(guide to understand the fields and indicators provided in the working papers) and CAATs working paper will be made available to explain the process followed, as well as the objective of the CAATs performed and will be referenced to the applicable procedures and the file abbreviations used.

Examples of files to be made available to regularity auditors:

- Employees with invalid identity numbers or incorrect surnames compared to the national population register
- Employees deceased and still on payroll
- Determination of bank account changes and number thereof.

4.2. Roles and responsibilities

The identification of risks is performed holistically by ARD for the whole of employee cost as part of the horizontal audit.

Regularity auditors are required to add additional inherent risks, as identified as part of the overall planning stage and to substantiate exceptions generated.

ISA is responsible for the development, processing and distribution of CAATs. ISA will provide the CAATs manual and CAATs working paper for inclusion in the audit file. CAATs will be provided for six-, nine- and 12-month periods.

ISA performs the walkthroughs on the Persal automated controls included in the business processes.

4.3. Impact of the horizontal approach

Fewer hours are spent on the audit of employee cost and efficiencies are gained. The quality of the audit procedures is centrally monitored through the development of CAATs and associated working papers. Reporting on employee costs will be more consistent.

This approach eliminates the need for ad hoc audit procedure design and different approach having to be followed for the same system and similar business processes.

5. Supply Chain Management Analytics

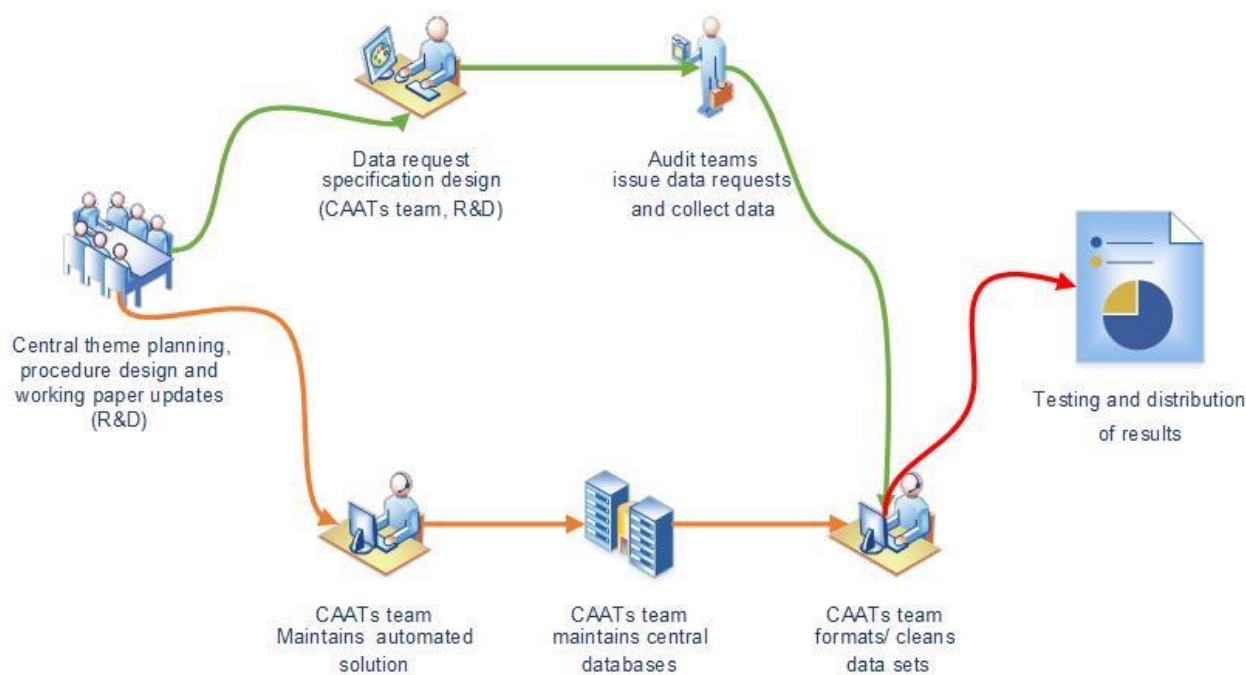
The AGSA adopted the ISSAI 1240 approach whereby it is assumed that there is a significant risk of fraud in public sector procurement processes. The practice note deals with the auditor's responsibilities relating to fraud in an audit of financial statements. Significant numbers of auditees displayed the following fraud indicators:

- Payments made to fictitious suppliers
- Awards made to persons in service of the auditee
- Non-disclosure of interest by persons that benefited from awards
- Non-disclosure by suppliers of their connections to persons in service of the state
- Non-disclosure of awards to close family members of persons in service of the auditee
- Payments made to prohibited suppliers.

5.1. Approached followed

The AGSA conducts procurement data analytics for 1 037 audits annually. To do so, a horizontal/cross-cutting audit theme was put in place, the implication being that the same audit procedures will be carried out to address the inherent risks identified for the audit of the procure-to-pay business process. The audit response has also been standardised, with the result that the audit procedures are the same for all audits that are fully supported by data analytic tests.

This scenario can only be accomplished by having an automated data analytics solution in place. However, although the AGSA's data analytics test solution is automated, data gathering is not automated and requires extensive manual intervention. The illustration below explains the steps of the solution, with a brief explanation of the relevant sections.



Central theme planning, procedure and working paper updates

The AGSA is currently using the horizontal auditing process as central theme for the auditing of procurement and contract management. Horizontal auditing is a process whereby a single business unit or team performs audit processes and procedures that are common to a number of engagements with a predetermined focus.

The objectives of performing a horizontal audit are typically to:

- increase audit efficiency – decreasing the audit time while still meeting professional standards
- improve the quality of audit procedures
- improve consistency between engagements, which promotes consistent reporting
- increase value-for-money audit procedures in engagements.

Data request specification design

The Companies and Intellectual Property Commission (CIPC) database is the only central database used for the testing. CIPC was established by the Companies Act, 2008 (Act No. 71 of 2008) as a juristic person to function as an organ of state within the public administration, but as an institution outside the public service. The main functions of the Commission are as follows:

- Registration of companies, cooperatives and intellectual property rights (trademarks, patents, designs and copyright) and maintenance thereof
- Disclosure of information on its business registers

- Promotion of education and awareness of company and intellectual property law
- Promotion of compliance with relevant legislation
- Efficient and effective enforcement of relevant legislation
- Monitoring compliance with and contraventions of financial reporting standards, and making recommendations in this regard to Financial Reporting Standards Council (FRSC)
- Licensing of business rescue practitioners
- Report, research and advise the Minister on matters of national policy relating to company and intellectual property law.

All other data required for testing is individually obtained as each government department or entity owns and manages its systems independently. Also, there is no standard system that is used across all the departments and entities and the AGSA does not have remote access to these systems. This presented a huge challenge in obtaining the data.

The CAATs team analyses relevant intended audit procedures and develops a technical specification for the data requirements, basically standardising the data/fields to be provided. Critical fields are indicated by a “high requirement” rating, which means that these fields are needed to achieve the desired outcome and are non-negotiable. The less critical fields are added as they allow tests of a better quality to be performed. The following fields are required:

Priority	Field
A. Source: Payroll system	
Scope: All employees (including accounting officer/ members of accounting authority) and political office bearers (POB) of auditee in service in the current financial period.	
High	Identity number (ID)
High	Name/ initials and surname
Medium	Banking account details
Medium	Address
Medium	Telephone number
Low	Position (management level) and job title
Low	Personnel number
Low	Appointment and resignation dates
Low	Section/component where employee works
B. Source: Financial system	
Scope: All suppliers that received payments in current financial period	



Priority	Field
High	Supplier name
Medium	Entity number
Medium	Vat number
Medium	Banking account details
Medium	Address
Medium	Telephone number
Medium	Total payments to supplier in current financial year
Low	Supplier number

Data request specification design

A request for information is issued to the relevant accounting authority. The data is collected by the responsible audit team and sent to the CAATs team for the applicable analysis.

CAATs team maintains automated solutions

Based on the central theme planning, procedures might change. The CAATs team ensures that the automated solutions include the necessary information to address current audit procedures.

CAATs team maintains central database

A central database containing all details of employees and suppliers used by all government entities is created and maintained through the process. It is also important that information used for comparisons is up to date in order to ensure complete and accurate results.

CAATs team formats / cleanses data sets

Data quality is a challenge, as well as the format in which it is received. Although the data format is specified, 20% of the data received is not in the correct format. The data analytics team receives the specified data sets via email and then manually normalises it to meet the requirements for automated testing. This is an intensive process that requires various technical skills to be applied to transform the data into useable format.

Testing and distribution of results

Once the data has been formatted into the automated solution standard, testing proceeds as explained in the guide and the results are made available to the audit teams. The automated solution provides reports for the following:

- Identification of fictitious suppliers:



- Employees who shared bank account details with suppliers
 - Employees who share the following details with suppliers:
 - a) Street addresses
 - b) Postal addresses
 - c) Telephone numbers
 - Duplicate supplier information, based on the criterion that a supplier has the same address, telephone numbers and VAT numbers, but has different bank account details
 - Suppliers with no physical address, only a postal address
 - Supplier with no Vat numbers.
- Awards were made to persons in service of the auditee
 - Awards were made to a person's family members in service of the auditee
 - Suppliers declared the interest
 - Identify awards made to suppliers that are prohibited from doing business with the state
 - Identify awards made to private companies or close corporations (CCs) that have been liquidated or deregistered
 - Identify awards made to shelf companies, based on the supplier name
 - Identify awards made to companies that were registered in the past year.

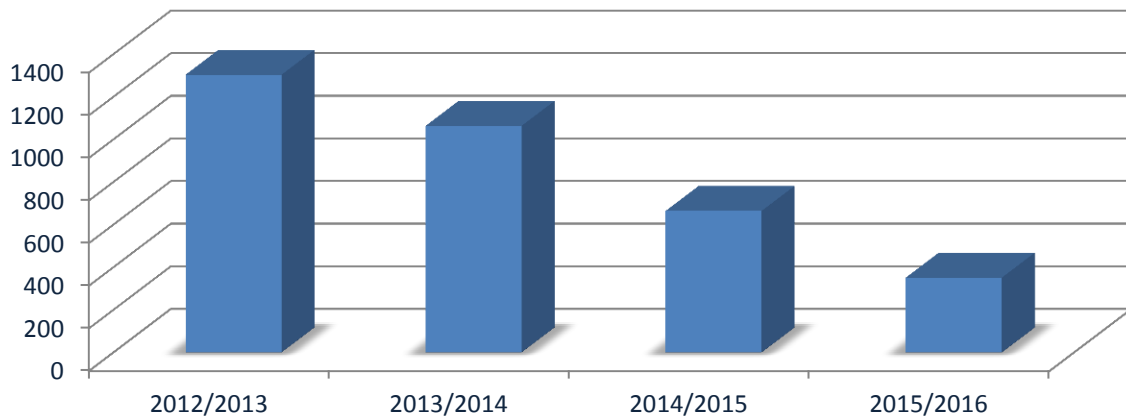
5.2. Impact of the horizontal approach

After completion of all audits for the applicable audit cycle, the AGSA issues a consolidated general report on national and provincial audit outcomes, which focuses on key areas. Part of this report focuses on the status of financial management. This section includes findings relating to irregular expenses caused by weakness in supply chain management. It focuses on the following three areas:

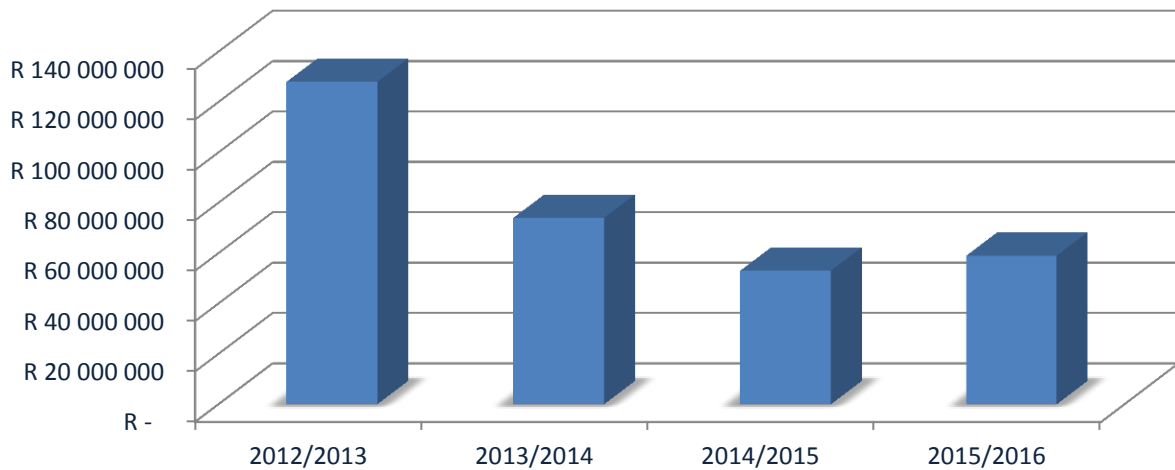
- i) Awards that were made to persons in service of the auditee
- ii) Awards that were made to a person's family members in service of the auditee
- iii) Awards that were made to a supplier in which government employees have an interest. The suppliers did not declare their interest.

The following graphs indicate findings in this regard for the past four audit cycles:

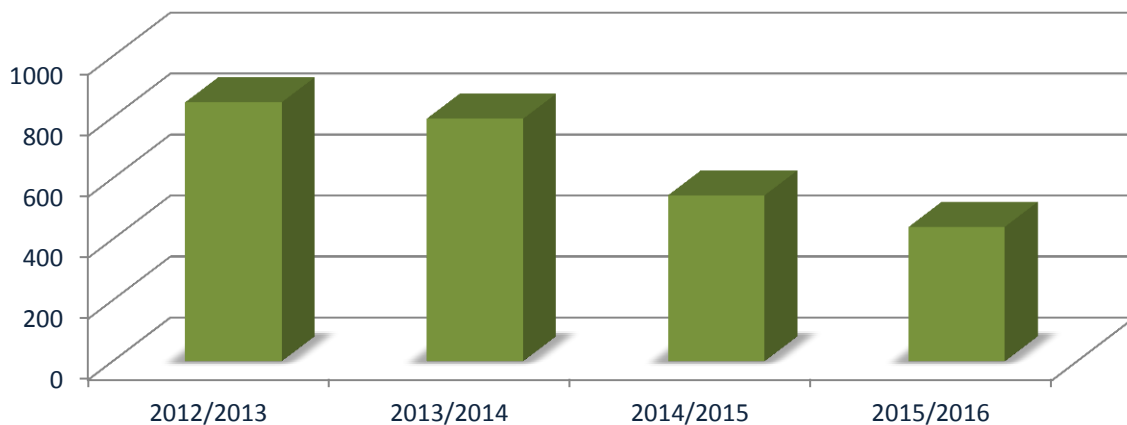
Awards that were made to persons in service of the auditee (number of instances)



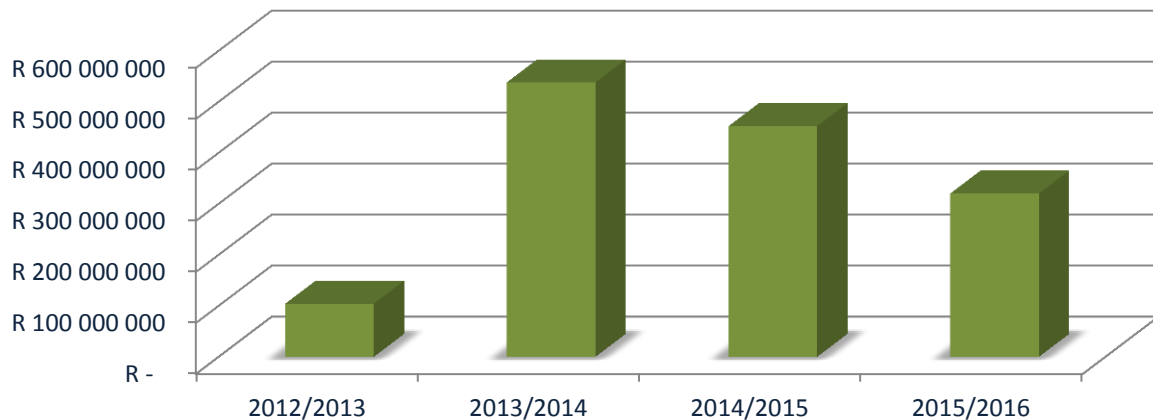
Awards that were made to persons in service of the auditee (value)



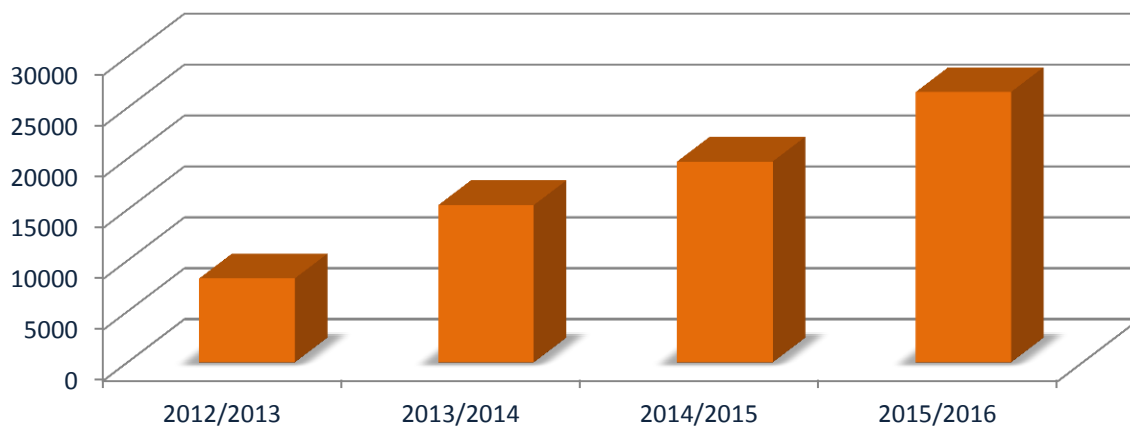
Awards that were made to a person's family members in service of the auditee (number of instances)



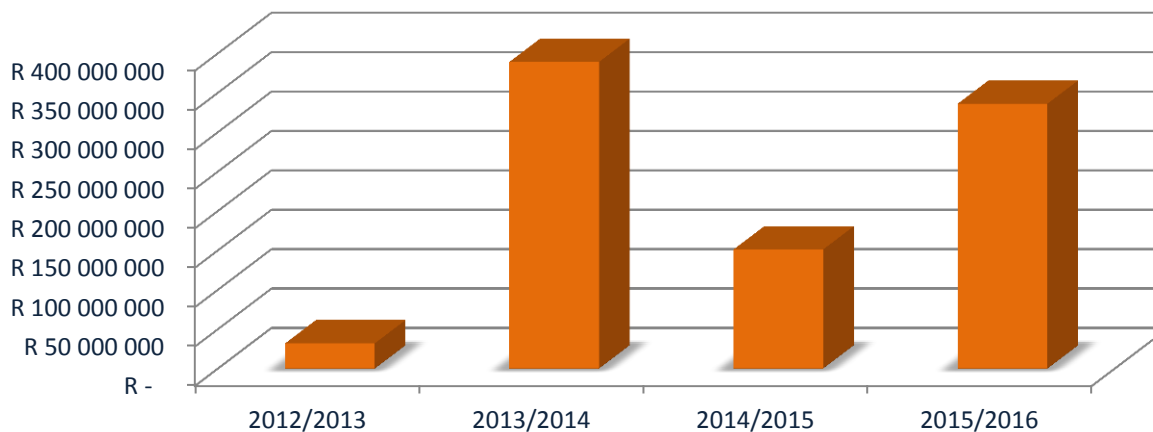
Awards that were made to a person's family members in service of the auditee (value)



Awards that were made to suppliers, in which government employees have an interest (number of instances)

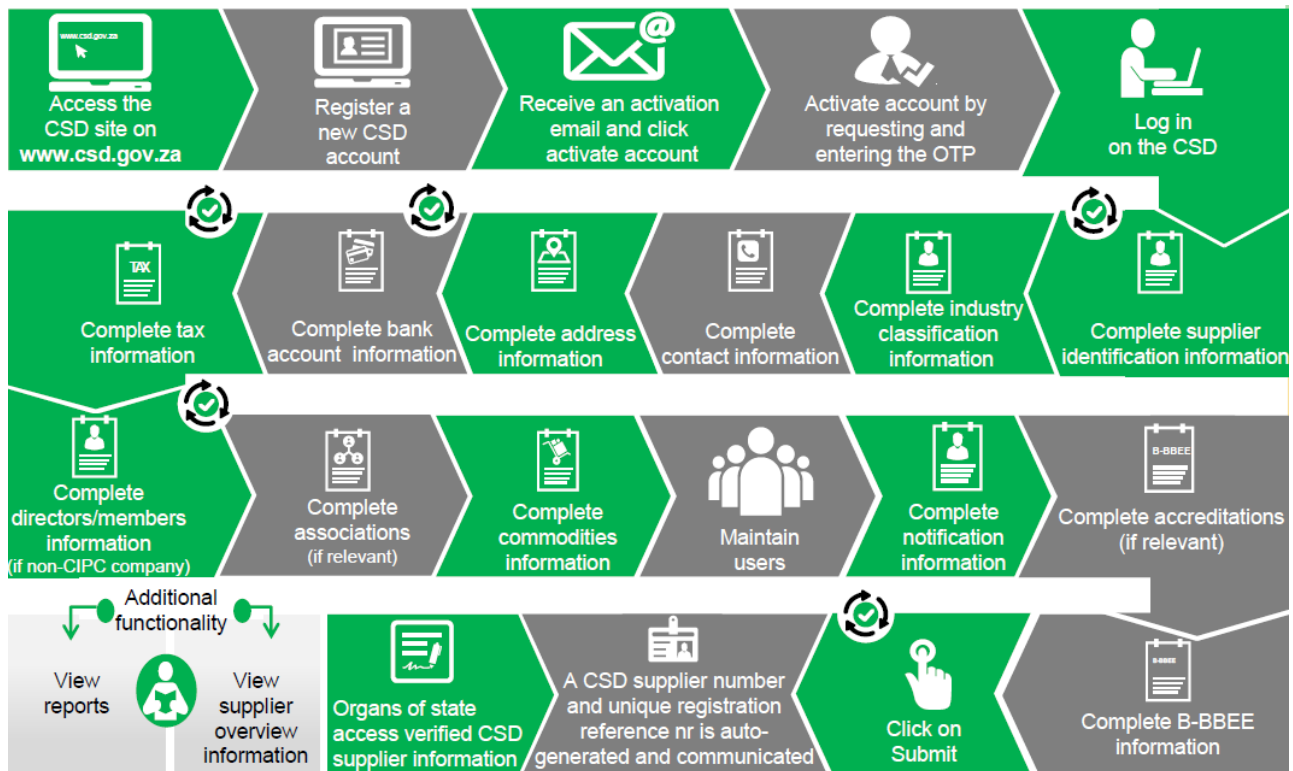


Awards that were made to suppliers, in which government employees have an interest (value)



It total, payments to the value of **R2 636 million** were identified. These figures had a mayor influence on the way that government does business.

A Central Supplier Data was implemented on 1 April 2016. The Central Supplier Database maintains a database of organisations, institutions and individuals who can provide goods and services to government. The process consists of the following:



During the process proper vetting ensures that the risk identified by the AGSA is limited.

Due to the finding raised by the auditor-general, regulations were amended after President Jacob Zuma signed the Public Administration Management Act in 2014, which also compels state employees to disclose their financial interests. The act states the following:

“9. (1) an employee must, in the prescribed manner, disclose to the relevant head of the institution all his or her financial interests and the financial interests of his or her spouse and a person living with that person as if they were married to each other, including all—

- (a) Shares and other financial interests in an entity;
- (b) Sponsorships;
- (c) Gifts above the prescribed value, other than gifts received from a family member;
- (d) Benefits; and
- (e) Immovable property.

(2) Failure by an employee to comply with the obligation referred to in subsection (1) constitutes misconduct.”

6. Conclusion

The Auditor-General of South Africa continuously strives for improvements that will add value to stakeholders. The enhancement of the audit process for employee cost and supply chain management was part of the initiative to ensure that we supply a valuable and relevant product. It ensures:

- accountability
- good governance
- ethical behaviour

and ultimately promotes democracy and good governance in South Africa.