

# **Report of the Auditor-General on a**

performance audit of entities that  
are connected with government  
employees and doing business  
with departments of the Western  
Cape Provincial Administration

**A u g u s t 2 0 0 8**



# TABLE OF CONTENTS

TITLE	PAGE
1. Executive summary	2
2. Purpose and content of the report	3
3. Audit scope	4
4. Modus operandi	5
5. Scope exclusion	6
6. Overview of employee-related companies and/ or close corporations (CCs) doing business with departments of the Western Cape Provincial Administration	6
7. Findings, recommendations and comments from departments	7
7.1 Performance of remunerative work	7
7.2 Declaration of interest on standard bidding documentation	11
7.3 Deviation from the supply chain management process	13
8. Appreciation	20
<b>Abbreviations</b>	21
<b>Annexure A:</b> Employee-related companies and CCs doing business with own departments	22
<b>Annexure B:</b> Employees' spouse-related companies and CCs doing business with own departments	23
<b>Annexure C:</b> Employee-related companies and CCs doing business with other departments in the Western Cape Provincial Administration	24

# **REPORT OF THE AUDITOR-GENERAL ON A PERFORMANCE AUDIT OF ENTITIES THAT ARE CONNECTED WITH GOVERNMENT EMPLOYEES AND DOING BUSINESS WITH DEPARTMENTS OF THE WESTERN CAPE PROVINCIAL ADMINISTRATION**

## **1. EXECUTIVE SUMMARY**

1.1 The Auditor-General issued a report to Parliament in January 2006 on the approval for government employees to perform other remunerative work and the disclosure of financial interests by ministers, deputy ministers and senior managers. This report indicated that designated employees (senior managers) and certain ministers failed to declare their interests and that the majority of government employees did not have approval to perform remunerative work outside their employment in government as prescribed by the relevant legislation and regulations.

1.2 Based on the above, a transversal performance audit was conducted on government employee-related entities doing business with national and provincial departments.

1.3 During the audit specific emphasis was placed on:

1.3.1 performance of remunerative work

1.3.2 declaration of interest in standard bidding documentation (SBD)

1.3.3 deviation from the supply chain management process.

1.4 The audit revealed, inter alia, the following:

1.4.1 The extent of business done by employee- or spouse-related companies in the Western Cape Provincial Administration for the period 1 April 2005 – 31 March 2007 amounted to approximately R60 million. The majority of employees did not have approval to perform other remunerative work.

1.4.2 Tenderers made misrepresentations by not declaring in the tender documentation that employees are related to the companies and CCs that are tendering.

1.4.3 The following transversal findings were made where departments of the Western Cape Provincial Administration deviated from the supply chain management process without the necessary approval and awarded tenders or quotations to employee-related entities. This could be an indication of preferential treatment of such employee-related entities or of fraudulent activities in the awarding of tenders or contracts.

(a) Provincial departments did not always obtain three quotations for transactions

with a value above R10 000 but not exceeding R200 000 in line with the regulations for the procurement of goods and services.

- (b) In certain instances provincial departments did not invite competitive bids for procurement where the value of the goods or services exceeded R200 000, in accordance with the regulations, and awarded the contracts to employee-related entities.
- (c) Provincial departments awarded bids to employee-related entities that did not score the highest points during the evaluation process, without providing reasonable and justifiable grounds for doing so.

1.5 There are inconsistencies between departments in rectifying the above shortcomings. In some instances departments charged employees with misconduct and discharged the employees or issued final warnings, while others indicated that disciplinary steps could not be taken as employees were not aware that they should have obtained approval to perform other remunerative work. A consistent approach, which includes awareness, training, disciplining and legal action as well as the blacklisting of entities, should be encouraged.

1.6 In response to the findings made by the Auditor-General, the Accountant-General, the Public Service Commission (PSC) and the Department of Public Service and Administration (DPSA) indicated that the current legislation and regulations would be reviewed and consideration would be given to amending them, if necessary, to limit and avoid the shortcomings identified in this report.

## **2. PURPOSE AND CONTENT OF THE REPORT**

2.1 A performance audit was conducted of entities that are connected with government employees and are doing business with departments of the Western Cape Provincial Administration, as per section 188(4) of the Constitution of the Republic of South Africa, read in conjunction with sections 5(3) and 20(3) of the Public Audit Act, 2004 (Act No. 25 of 2004). The purpose of this report is to facilitate public accountability by bringing to the attention of the provincial legislature the findings of the performance audit.

2.2 Sufficient audit work was performed to provide substantiating audit evidence for the findings set out herein.

2.3 It is anticipated that this report, which reflects comments received from various departments, would give rise to corrective steps that would contribute constructively to the establishment and implementation of appropriate management measures and controls, and consequently to improved value for money.

- 2.4 The responsibility for instituting these management measures rests with management. The primary objective of performance auditing is to confirm independently that these measures do exist and are effective, and to provide the executive and legislative bodies with findings and examples of the effects thereof, by means of a structured reporting process.

### **3. AUDIT SCOPE**

- 3.1 This performance audit focused on the following aspects:

3.1.1 Employees of departments of the Western Cape Provincial Administration who are directors or members of the companies and CCs that did business with the departments where such employees work (annexure A refers).

3.1.2 Transactions by employees' spouses who are directors or members of companies and CCs that did business with departments where the husband/wife is employed (annexure B refers).

3.1.3 Employees of departments who are directors or members of companies and CCs that did business with other departments of the Western Cape Provincial Administration (annexure C refers).

3.2 The transactions included in this report cover the period 1 April 2005 to 31 March 2007 unless stated otherwise.

3.3 The scope was limited to the procurement process up to the approval of the payments. The scope also included determining whether employees who had an interest in the company or CC that rendered the service or supplied the goods to the department were involved in the procurement process.

3.4 The objective of the performance audit was to identify companies and CCs that are primarily profit driven and are transacting with departments. For this reason the following types of companies were excluded from the scope of the performance audit:

3.4.1 Section 21 (not for profit) companies as defined in the Companies Act, 1973 (Act No. 61 of 1973).

3.4.2 Public entities listed under the Public Finance Management Act, 1999 (Act No. 1 of 1999) (PFMA).

3.4.3 Companies where the person is appointed as an independent contractor or board member in an executive capacity at a department. The reason for this is that in those

cases the person's details are loaded on the Personnel and Salary System (Persal) for income tax purposes, and not because he/she is a permanent employee of the department.

3.4.4 Employees who hold shares in listed companies.

3.5 The objectives of the procedures performed were the following:

3.5.1 To identify the extent of employee-related entities that did business with departments of the Western Cape Provincial Administration

3.5.2 To enhance transparency and adherence to relevant legislation

3.5.3 To identify and report on findings in the current processes and systems

3.5.4 To possibly reduce the risk of corruption.

#### **4. MODUS OPERANDI**

4.1 Performance audits are conducted in accordance with the internal guidelines for the planning, execution, reporting and follow-up of performance audits.

4.2 Computer-assisted audit techniques (CAATs) were used extensively to compile exception reports, while procedures were developed for following up on these exceptions. The following databases were used in the compilation of exception reports during the performance audit:

4.2.1 Database of the Companies and Intellectual Property Registration Office (CIPRO) database of directors of companies and members of CCs as at 31 March 2006. Actual dates of appointments and resignations were confirmed with CIPRO.

4.2.2 Persal payroll data for March 2006.

4.2.3 Consolidated Basic Accounting System (BAS) payment data for the period 1 April 2005 to 31 March 2007, unless stated otherwise. This file included accounts payable data for government departments on BAS during this period.

4.3 The relevant supporting documentation was requested from the departments and audited. After the performance audit of each of the departments had been finalised, a management letter/report with findings was submitted to the department for comments. The comments received were considered and incorporated in this report.

## **5. SCOPE EXCLUSION**

- 5.1 The scope of the performance audit did not include the verification of shares held in companies, as this information is not available on the CIPRO database. Consequently, where an individual resigned as a director of a company, it was not possible to confirm that the employee had also sold his/her shares in the company unless this was discovered by chance. Therefore, a risk exists that employees might have resigned as directors from companies, but had not sold their shares in the companies. If the shareholding was not declared, or the employee had not requested permission to perform other remunerative work outside his/her employment at the department, it was not possible to identify employees who held shares in companies that conducted business with departments of the Western Cape Provincial Administration.
- 5.2 Similarly, the procedures conducted in this performance audit will not reveal collusion between employees employed at a department and the company that did business with the department. This relates to employees who may be receiving another form of gratuity or emolument from the company that did business with the department.

## **6. OVERVIEW OF EMPLOYEE-RELATED COMPANIES AND/OR CCs DOING BUSINESS WITH DEPARTMENTS OF THE WESTERN CAPE PROVINCIAL ADMINISTRATION**

- 6.1 During the performance audit a significant number of cases were identified where the employee had resigned as a director or member of the company or CC. This could possibly be attributed to the impact of the Report of the Auditor-General on the declarations of interest by ministers, deputy ministers and government employees that covered the 2004-05 financial year [RP 19/2006]. Where the employee had resigned before the transaction occurred, the information was omitted from the final summary. The following table is a summary of the number of employees, number of companies and/or CCs and amounts paid to companies or CCs that transacted with the departments. Refer to annexures A to C for details.



## Summary of employee-related companies and/or CCs doing business with departments of the Western Cape Provincial Administration

	Number of employees	Number of entities	Amount paid 01/04/2005 – 31/03/2007	Annexure
Employee-related companies and/or CCs doing business with own departments	25	25	51 704 389	A
Employees' spouse-related companies and/or CCs doing business with own departments <i>(Note)</i>	6	6	2 407 925	B
Employee-related companies and/or CCs doing business with other departments of the Western Cape Provincial Administration	40	40	5 599 547	C

**Note:** This exception report was compiled to audit the procurement process followed in awarding tenders/contracts to spouse-related companies and/or CCs

## 7. FINDINGS, RECOMMENDATIONS AND COMMENTS FROM DEPARTMENTS

### 7.1 Performance of remunerative work

Regulations with respect to remunerative work performed by government employees differ in certain instances between departments of the Western Cape Provincial Administration. Where relevant, these differences were taken into account.

#### 7.1.1 Regulations

- (a) Chapter VII, sections 30 and 31 of the Public Service Act of 1994 (Act No. 103 of 1994) (PSA) stipulates: *Unless it is otherwise provided for in his or her conditions of employment every officer and employee shall place the whole of his or her time at the disposal of the State. No officer or employee shall perform or engage himself or herself to perform remunerative work outside his/her employment in the public service, without permission granted by the relevant executing authority or officer authorised by the said authority. If an officer receives any remuneration, allowance or other reward, other than in accordance with this act, an amount equal to such remuneration received should be paid into the revenue account.*
- (b) Chapter 7, section 33 of the Employment of Educators Act, 1998 (Act No. 76 of 1998) states: *Unless an Educator's conditions of service provide otherwise, an educator shall place such time as the Minister may determine at the disposal of the Employer; no educator shall without permission of the employer perform or undertake to perform remunerative work outside the educator's official duty or work.*

- (c) Circular H41/2001 issued by the Department of Health in regard to the revised measures and procedures for the performance of remunerative work outside the public service states: *The policy is applicable to all employees appointed on a permanent basis, either full-time or part time as well as employees appointed for a period longer than 12 months in terms of a continuous employment contract or fixed term contract on the fixed establishment of the Health Department. However, employees appointed on a casual basis (temporary employment contract) or sessional basis (fixed term contract) may perform RWOPS without obtaining authority from the department of Health to perform such work.*
- (d) The *Explanatory Manual on the Code of Conduct for the Public Service* (a practical guide to ethical dilemmas in the workplace), paragraph 4.5.5, with regard to employees who undertake remunerative work outside their official employment without approval, states: *Employees are expected to place their undivided attention, time and skills at the disposal of the public service as employer. The nature and demands of the job in the public service are such that the interests of both the public service and community may be prejudiced by a public servant undertaking remunerative work outside official duties. It is therefore mandatory to obtain prior approval to perform remunerative work outside official hours.*

#### 7.1.2 Findings

- (a) A total of 25 employees were identified who are directors or members of companies or CCs that did business with the provincial department where the person is employed (annexure A refers). With respect to obtaining approval to perform remunerative work, it was found that none of these employees, as verified by the respective departments, had obtained approval to perform other remunerative work. The total amount paid to these companies and CCs during the period under review was R51,7 million.
- (b) In addition, 40 employees were identified who are directors or members of companies or CCs that did business with other provincial departments (annexure C refers). With respect to obtaining approval to perform remunerative work, it was found that three of these employees had obtained approval to perform other remunerative work. The total amount paid to these companies and CCs during the period under review was R5,6 million.
- (c) Three employees of the **Department of Education** who are members of CCs did business with the department to the value of R7 800 853. These employees did not place all their time at the disposal of the state, as stipulated in section 30 of the Public Service Act and the *Code of Conduct for the Public*

Service, as they were directly involved in the day-to-day operations of the CCs. Indicators that employees were involved in the day-to-day operations of the CCs are as follows:

- (i) Employees were managers of the entities and a percentage of the contract values were managed or executed by these employees;
- (ii) Quotations were faxed by employees during working hours; and/or
- (iii) Employees indicated their names and cell phone numbers on the quotations.

### **7.1.3 Recommendations by the Auditor-General**

- (a) As indicated in paragraph 7.1.2(a) and (b) above, only a few employees had requested and received approval to perform other remunerative work. Therefore the relevant departments should take disciplinary action against employees whose companies or CCs did business with the departments of the Western Cape Provincial Administration but had not requested approval to perform other remunerative work.
- (b) The departments should implement action plans to monitor the progress made with disciplinary action taken against employees who had not applied for and received approval to perform other remunerative work. The departments should also report back to the provincial legislature on the outcomes of the disciplinary action and the action plans implemented.
- (c) The departments should monitor on a yearly basis the extent of business conducted by their employees. If it is found that the extent of business conducted by these entities is excessive and impacts on the employees' ability to perform their duties at the departments, the departments should consider withdrawing the approval granted. Approval to perform other remunerative work should not be granted if an executive authority is certain that the approval would lead to work being performed for a government department.
- (d) The departments should implement and actively monitor the systems of control to manage the performance of other remunerative work by employees. This could include the annual issuing of letters to employees informing them of the requirement to obtain approval to perform other remunerative work. Copies of the letters of approval should be either kept centrally or placed on the employees' files. Where possible, the completeness of certain aspects of the declarations should also be verified by, for example, conducting CIPRO searches to confirm the completeness of the declared directorships and memberships of companies and/or CCs.

- (e) Designated employees (senior managers) should be informed of the requirement that they should also request approval to perform other remunerative work. The fact that disclosure in the financial disclosure forms is not sufficient, should be emphasised.
- (f) Companies should be requested to supply their shareholding, and not just directorship, in the tender documentation to allow departments to identify related-party transactions.
- (g) Consideration should be given to amending the existing regulations with regard to the declaration of interests and the performance of other remunerative work by government employees as follows:
  - (i) Non-designated employees (levels one to 12) who hold directorships or memberships of companies and/or CCs should disclose such directorships and memberships. According to the DPSA, the possibility of extending the system to non-designated employees and supply chain management officials had been considered before and it was decided not to extend the system. However, in light of the recommendations and findings made in this report, the extension of the system should be reconsidered.
  - (ii) Non-designated and designated employees should specifically disclose details of directorships and memberships of companies and/or CCs that had previously transacted with government. An overview of the transactions with government should also be provided.
  - (iii) Non-designated and designated employees should disclose their spouses' directorships and memberships of entities that are transacting with the specific government institution where they are employed.
- (h) Newly appointed government employees should make the disclosures within 30 days of appointment, while government employees who are transferred from one government department to another should again make the required disclosures at the new department within 30 days of transfer.
- (i) The policy should require government employees to disclose changes in circumstances that could have an impact on the completeness or accuracy of the declarations they had provided. Such disclosure should be made within 30 days of the change in circumstances. For example, a newly acquired directorship or membership should be disclosed by a government employee within 30 days of obtaining it.
- (j) Non-designated and designated employees should take personal responsibility for ensuring that CIPRO processes their resignation/termination of directorships and memberships.

#### 7.1.4 Responses from provincial departments

- (a) The **Department of Education** has noted the findings. The department is also considering disciplinary action against employees who did not have approval to perform other remunerative work.
- (b) The **Department of Health** will ensure that the necessary control measures are instituted. In the case where permanent staff did not have approval to perform remunerative work outside public service, the department will apply the *audi alteram partem* (employees will be given the opportunity to present their side of the situation before disciplinary action is taken) ruling and thereafter will consider taking disciplinary action against the employees.
- (c) The **Western Cape Provincial Parliament** could not take any disciplinary action against the employee as the employee had left the service of the department.
- (d) The **Department of Social Development's** comments only indicated whether the employees had approval to perform remunerative work and did not address the corrective measures to be implemented.
- (e) The **Department of Cultural Affairs and Sport** could not take any disciplinary action against the employee as the employee had left the service of the department.
- (f) The **Department of Transport and Public Works'** comments only indicated whether the employees had approval to perform remunerative work and did not address the corrective measures to be implemented. Due to the fact that some of the employees had left the service of the department, no disciplinary action could be taken against such employees.

## 7.2 Declaration of interest on standard bidding documentation

### 7.2.1 Regulations

- (a) The declaration of interest form (WCBD 4) issued as part of the standard bid documentation, paragraph 2, requires the bidder to make the following declarations:
  - 2.1 *Are you or any person connected with the bidder, employed by the principal?*
  - 2.2 *Do you, or any person connected with the bidder, have any relationship (family, friend, other) with a person employed by the principal and who may be involved with the evaluation and/or adjudication of this bids?*

2.3 Are you, or any person connected with the bidder, aware of any relationship (family, friend, other) between the bidder and any person employed by the principal who may be involved with the evaluation and/or adjudication of this bids?

- (d) Paragraph 2.8.1: Fraud and Corruption of the supply chain management document – a *Guide for accounting officers / authorities* defines “fraudulent practice” as a *misrepresentation of facts in order to influence a selection process*.
- (e) Paragraph 23 of the general conditions of the contract states: *The purchaser, without prejudice to any other remedy for breach of contract, by written notice of default sent to the supplier, may terminate this contract in whole or in part if the supplier, in the judgement of the purchaser, has engaged in corrupt or fraudulent practices in competing for or in executing the contract.*

## 7.2.2 Findings

- (a) Various instances were identified where entities misrepresented facts on the WCBD 4 declaration of interest form by not declaring the financial interest of employees of a department and/or their spouses who were directors or members of companies or CCs. Close relatives of employees certified that the information furnished in the WCBD 4 was correct. By signing the tender documents the bidders accepted that the department may act against them in terms of paragraph 23 of the general conditions of the contract should the declaration prove to be false. Entities were subsequently awarded tenders although close relatives had misrepresented the facts in the bid documentation which could have influenced the selection process. A summary of transactions and the number of entities that had not provided correct information is set out below per department.

Misrepresentations on WCBD 4 declaration of interest form		
Departments	Number of entities	Transaction amount R
Education	3	8 331 196
Health	1	34 975 618
<b>Total</b>	<b>4</b>	<b>43 306 814</b>

## 7.2.3 Recommendations by the Auditor-General

The department should investigate the contracts awarded to the entities that had made false declarations of interests in their bidding documents and the department should consider cancelling contracts with these entities. The department should furthermore consider blacklisting these entities at National Treasury.

#### 7.2.4 Responses from provincial departments

- (a) The **Department of Education** will refer the cases to the departmental legal adviser for advice on possible cancellation of the contracts as these contracts were still in operation.
- (b) The **Department of Health** indicated that the case would be reported to the Bid Committee for a decision regarding further action against the CC.
- (c) In this regard the **Accountant-General** also responded as follows:
  - (i) The declaration of interest form should be amended to also indicate the position occupied by the shareholder/director/member in the department, as well as the name of the department. Directors/members/shareholders of companies tendering should also declare their interests in other related companies, whether or not such related companies are tendering.
  - (ii) Spouses' directorship/shareholding/membership in companies that had transacted with the state in the 12 months of the past financial year should be declared. A database of all closed projects, with their performance results, should be kept and where subsequent tendering is received from companies that had previously tendered with government departments, reference to their previous performance should be made and the decision to award the tender should be influenced by the latter.
  - (iii) An integration of the PSC system and CIPRO should be considered. An investigation into whether the forms are kept manually or electronically will have to be conducted. If the system is manual, a feasibility study on whether to change from manual to electronic is recommended.

### 7.3 Deviation from the supply chain management process

#### 7.3.1 Inviting of bids

##### 7.3.1.1 Regulations

- (a) *Practice note no. SCM 2 of 2005 states: Accounting officers/ authorities should invite and accept written price quotations for requirements up to an estimated value of R200 000 from as many suppliers as possible, that are registered on the list of prospective suppliers. Furthermore, paragraph 3.3 states: If it is not possible to obtain at least three (3) written quotations, the reasons should be recorded and approved by the accounting officer/ authority or his/her delegate.*
- (b) The Department of Health issued delegations to the supply chain management functionaries in terms of section 44(1) of the PFMA, the Framework for Supply



Chain Management Regulations and the Provincial Treasury Instructions. Items 3 and 4 made provision for the *procurement of supplies or services, the hiring or letting of anything, the acquisition or granting of any right, resulting from telephonic or verbal informal bids which are obtained from possible suppliers* for contract values up to R5 000 and R50 000 respectively. A condition is that *the acceptable informal bid with the highest points must be accepted*.

### 7.3.1.2 Findings

- (a) Instances were identified where goods and services were procured without obtaining three written quotations from prospective suppliers. Reasons were not supplied and approved by the accounting officer/authority or his/her delegate for deviation from the regulations. There is a possible risk that other suppliers providing these goods and services may have been unfairly prejudiced as they had not been approached to provide quotations and the departments may have procured these goods and services at higher prices as alternative suppliers were not approached for quotations.

Three written quotations not obtained		
Departments	Number of instances	Transaction value R
Education	3	175 978
Health	1	31 400
<b>Total</b>	<b>4</b>	<b>207 378</b>

- (b) The **Department of Education** procured goods to the value of R274 717 from an entity in which an employee and his/her spouse have interests. The goods were procured at prices much higher than the current market price had items been bought over the counter. The market value of the goods at the time the department procured the items was R177 360. This is the direct result of not obtaining written quotations from as many suppliers as possible as indicated in paragraph 7.3.1.1(a).
- (c) **Department of Health**
- (i) The department acquired the services of nursing staff from two employee-related entities to the value of R19 200 170. From the payment documentation it could not be determined whether tenders had been invited.
  - (ii) The department procured services to the value of R575 773 from suppliers in which officials of the department have an interest without obtaining written quotations from prospective suppliers. Only the



invoices and/or statement or payment advice supplied by the employee-related entity were attached to the payment documentation.

#### 7.3.1.3 Responses from provincial departments

(a) The **Department of Education** indicated that:

- (i) Disciplinary action would be taken against the officials who had not obtained three quotations.
- (ii) Officials were aware that the lowest price quotations should be accepted and, if not, that reasons should be provided. Disciplinary steps would be taken against the officials who had not followed due process.
- (iii) In instances where quotations were obtained via the electronic purchasing system the issue would be taken up with the administrator of the system with a view to finding an acceptable solution. The possibility of re-advertising the service in instances of this nature would also be an option.

(b) The **Department of Health** indicated that:

- (i) The department will further investigate the appointment of nursing staff by, amongst others, contacting the supplier to obtain more information and supporting documentation. Should the relevant source documentation be obtained, it will be attached to the payment. In the event that the relevant source documents cannot be found, the payment will be disallowed and reported on as required in terms of the PFMA.
- (ii) The department has implemented measures to ensure that staff are retained and prevented from doing work outside the department by means of recruitment agencies.
- (iii) The department also indicated that very few nursing agencies exist in rural areas and that those in the metropolitan areas often cannot deliver a service to rural hospitals. They are usually more expensive due to travel and accommodation costs. The call for informal bids may very well result in only one such bid or none at all. All suppliers in the area are then utilised. Redistribution of nurses from other areas is not possible due to the shortage of nurses in these small hospitals. The filling of posts is continuously receiving attention, but there are too few nurses currently available in the market. The use of agency nurses has been managed down to a very low level in the rural areas over the past few years. Only in the face of real emergencies or crises are the services of agency nurses procured.

## 7.3.2 The evaluation process

### 7.3.2.1 Regulations

- (a) A circular issued by National Treasury dated 10 May 2005 pertaining to the evaluation of bids states: *A bid is regarded as acceptable if:*
  - (i) *It complies in all respects with the specification and conditions of the bid;*
  - (ii) *the bidder completed and signed all the prescribed bid forms to enable the principal to evaluate the submitted bid;*
  - (iii) *the bidder submitted the required original tax clearance certificate and other clearance/ registration forms as prescribed by the various acts and/ or in the bid documentation; and*
  - (iv) *the bidder has the necessary capacity and ability to execute the contract.*
- (b) Furthermore the circular states that *bids may only be evaluated in accordance with the evaluation criteria stipulated in the bid documentation. When any bids is passed over or regarded as non-responsive, the reason for passing over such bid must be defensible in any court of law.*

### 7.3.2.2 Findings

One instance was identified where the **Department of Education** awarded a tender to the value of R294 978 to a security company. The bid evaluation committee disqualified an entity with a tender price of R261 048 without giving valid reasons and awarded the tender to an employee-related entity. This could be an indication of preferential treatment of such entity. Furthermore, the department could have saved R33 930 by not disqualifying the tenderer with the lowest acceptable price.

### 7.3.2.3 Responses from the Department of Education

The department will write off the R33 930 as an irregular expenditure. To prevent a similar occurrence in future, the Supply Chain Management Unit will be instructed by the relevant consideration committees during the evaluation and adjudication processes to ensure that both the name under which an entity tenders as well as all their trading names, where applicable, are indicated in full in the bid document as well as in the relevant memoranda. In doing this, the bid evaluation committee, as well as the delegated official, will have the necessary information at their disposal to make an informed decision.

### 7.3.3 Restrictive horizontal practice

#### 7.3.3.1 Regulations

The Competition Act, 1998 (Act No. 89 of 1998), chapter 2, paragraph 4 states as follows: *Restricted horizontal practices prohibited.* –

- (1) *An agreement between, or concerted practice by, firms, or decision by an association firm, is prohibited if it is between parties in a horizontal relationship and if –*
  - (a) *it has the effect of substantially preventing, or lessening, competition in a market, unless a party to a agreement, concerted practice, or decision can prove that any technological, efficiently or other pro-competitive gain resulting from it outweighs that effect; or*
  - (b) *it involves any of the following restricted horizontal practices:*
    - (i) *directly or indirectly fixing a purchase or selling price or any other trading condition;*
    - (ii) *dividing markets by allocating customers, suppliers, territories, or specific types of goods or services; or*
    - (iii) *collusive tendering.*
- (2) *An agreement to engage in a restrictive horizontal practice referred to in subsection (1)(b) is presumed to exist between one or more firms if –*
  - (a) *any one of those firms owns a significant interest in the other, or they have at least one director or substantial shareholder in common, and*
  - (b) *any combination of those firms engages in that restrictive horizontal practice.*
- (4) *For purposes of subsections 2 “director” means -*
  - (a) *a director of a company as defined in the Companies Act, 1973;*
  - (b) *a member of a close corporation as defined in the Close Corporation Act, 1984;*
  - (c) *a trustee of a trust;*
  - (d) *a person holding an equivalent position in the firm.*

#### 7.3.3.2 Findings

The **Department of Education** procured goods/services to the value of R988 308 from two entities in which employees of the department have interests. In these instances quotations were supplied by individuals connected to the successful

suppliers. Therefore there may have been horizontal relationships between potential suppliers, which is prohibited because it has the effect of substantially preventing or lessening competition in the market. The following are indicators that the entities were engaged in restrictive horizontal practices as prohibited by the Competition Act, 1998 (Act No. 89 of 1998):

- (i) Two of the three written quotations were supplied by company representatives of the successful supplier;
- (ii) Quotations were sent from the same fax number at the same time;
- (iii) Layout, foot notes, thank-you notes and handwriting on quotations are similar;
- (iv) Suppliers had the same addresses, contact details and representatives; and
- (v) Entities that supplied quotations had identical entity and VAT numbers.

#### 7.3.3.3 Responses from provincial departments

The **Department of Education** indicated that the Directorate: Forensic Investigative Unit will be requested to investigate the cases mentioned. Depending on the outcome of this investigation disciplinary steps will be taken against the relevant officials or the necessary steps will be implemented against the relevant suppliers.

#### 7.3.4 Preferential treatment

##### 7.3.4.1 Regulations

- (a) Paragraph 1.3 of *Practice note no. SCM 4 of 2003* states: *Practitioners should be fair and impartial in the performance of their functions. They should at no time afford any undue preferential treatment to any group or individual or unfairly discriminate against any group or individual. They should not abuse the power and authority vested in them.*
- (b) Section 38 of the Public Finance Management Act, 1999 (Act No. 1 of 1999) confers general responsibilities on the accounting officers. Subsection 1 states that the accounting officer for a department *(a) must ensure that a department, trading entity or constitutional institutional has and maintains – an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective;.....*

##### 7.3.4.2 Findings

- (a) Five instances were identified where a sessional employee, in his capacity as a surgeon with a 100 per cent membership in an entity, supplied orthopaedic implants and prosthesis to the **Department of Health**. The choice of which supplier to use for procurement of orthopaedic implants and prosthesis rests

with the surgeon. The official was the responsible surgeon for the operations in these instances and consequently was directly involved in the procurement process of the orthopaedic implants and prosthesis. The orthopaedic implants and prostheses were purchased from a CC in which he held a 100 per cent interest. The total transaction value in this regard was R113 816. The total value of payments made to the employee-related entity was R4 479 474 for the period 1 April 2005 to 31 March 2007.

- (b) Tygerberg Hospital obtained nursing staff from three agencies for the period 1 April 2005 to 31 March 2007. Sixty-two per cent of the total payments were made to a supplier in which an official holds a 100 per cent interest. Therefore the possibility exists that the relevant nursing agency received preferential treatment during the procurement process for nursing staff, which is in contradiction to section 38 of the Public Finance Management Act.

<b>Payments made to three agencies for nursing staff</b>		
<b>Nursing agency</b>	<b>Amount paid by the department for the period 01/04/05 – 31/03/07 R</b>	<b>% of payments made to each agency</b>
Nursing Agency A (employee-related CC)	34 975 618	62%
Nursing Agency B	2 335 775	4%
Nursing Agency C	19 464 206	34%
<b>TOTAL</b>	<b>56 775 599</b>	<b>100%</b>

#### 7.3.4.3 Responses from the Department of Health

The department indicated that there were originally only a few agencies that could supply certain candidates to Tygerberg Hospital in accordance with their nursing personnel needs. Before 2004 the department arranged for tariff lists from the various suppliers. Initially nursing agencies B and C were used to supply nurses. During 2004 Tygerberg Hospital was approached by nursing agency A to utilise their services as well. They also supplied a pricing schedule. Initially nursing agency A was only used in the two private wards in order to evaluate their performance. When nursing agencies B and C were unable to provide nursing staff, agency A was approached. Due to the increasing shortage of nursing staff, the requirements for agency personnel have increased drastically but at all stages the cheapest agency that could provide personnel was utilised. Due to price and availability of nursing personnel, use was increasingly made of nursing agency A's agency staff. During August 2006 the process was documented by Head Office by means of a flow diagram that was approved by the Head of Institution and the market was also tested at that stage.

## 8. APPRECIATION

- 8.1 The assistance of all role players involved during the performance audit is sincerely appreciated.

*Auditor-General*

Pretoria

August 2008



A U D I T O R - G E N E R A L

## ABBREVIATIONS

Word or phrase	Description
Auditor-General	(a) As an institution, means the institution contemplated in section 181(1)(e) of the Constitution; and (b) as an individual, means the individual appointed as Auditor-General, Mr Terence Nombembe.
BAS	Basic Accounting System
CAATs	Computer-Assisted Audit Techniques
CIPRO	Companies and Intellectual Property Registration Office
CC	Close corporation
Designated employee	Any person occupying a post on SMS grade C (13) in a national department
DPSA	Department of Public Service and Administration
Employee-related companies/CCs	Companies/CCs that are connected with government employees in terms of directorship or membership
Government employee	A person in the public service who holds a post on the fixed establishment of a state institution
Non-designated employee	Employees other than designated employees
Persal	Personnel and Salary System
PFMA	Public Finance Management Act, 1999 (Act No. 1 of 1999)
PPPFA	Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000)
PSA	Public Service Act, 1994 (Act No. 103 of 1994)
PSC	Public Service Commission
SCM	Supply chain management
SMS	Senior management staff
TR	Treasury Regulation
WCBD	Western Cape Bidding Document

**EMPLOYEE-RELATED COMPANIES AND CCs DOING BUSINESS WITH OWN DEPARTMENTS**

The table is a summary of employees who are directors or members of companies and/or CCs that did business with the departments where they are employed.

<b>List of employees doing business with their own department</b>					
<b>No.</b>	<b>Department</b>	<b>Number of employees</b>	<b>Number of entities</b>	<b>Amount paid for the period 01/04/2005 to 31/03/2007 R</b>	<b>Number of employees with approval already verified by departments</b>
1	Cultural Affairs and Sport	1	1	11 800	0
2	Education	6	6	8 459 744	0
3	Health	16	16	43 198 134	0
4	Local Government and Housing	0	0	0	n/a
5	Premier	0	0	0	n/a
6	Provincial Parliament	1	1	7 811	0
7	Social Development	0	0	0	n/a
5	Transport and Public Works	1	1	26 900	0
	<b>Total</b>	<b>25</b>	<b>25</b>	<b>51 704 389</b>	<b>0</b>



**EMPLOYEES' SPOUSE-RELATED COMPANIES AND CCs DOING BUSINESS WITH OWN DEPARTMENTS**

The table is a summary of employees' spouses who are directors or members of companies and/or CCs that did business with the departments where their spouses are employed.

<b>Employees' spouses doing business with departments where their spouses are employed</b>				
<b>No.</b>	<b>Department</b>	<b>Number of employees</b>	<b>Number of entities</b>	<b>Amount paid for the period 01/04/2005 to 31/03/2007 R</b>
1	Cultural Affairs and Sport	0	0	0
2	Education	4	4	2 355 566
3	Health	2	2	52 359
4	Local Government and Housing	0	0	0
5	Premier	0	0	0
6	Provincial Parliament	0	0	0
7	Social Development	0	0	0
8	Transport and Public Works	0	0	0
	<b>Total</b>	<b>6</b>	<b>6</b>	<b>2 407 925</b>

# **EMPLOYEE-RELATED COMPANIES AND CCs DOING BUSINESS WITH OTHER DEPARTMENTS IN THE WESTERN CAPE PROVINCIAL ADMINISTRATION**

The table is a summary of employees who are directors or members of companies and/or CCs that did business with other departments.

List of employees doing business with other departments					
No.	Department	Number of employees	Number of entities	Amount paid by other departments to employee-related entities for the period 01/04/2005 to 31/03/2007 R	Number of employees with approval already verified by departments
1	Cultural Affairs and Sport	0	0	0	n/a
2	Education	18	18	3 317 163	0
3	Health	17	17	648 487	0
4	Local Government and Housing	0	0	0	n/a
5	Premier	0	0	0	n/a
6	Provincial Parliament	1	1	72 577	0
7	Social Development	2	2	29 330	1
8	Transport and Public Works	2	2	1 531 990	2
	<b>Total</b>	<b>40</b>	<b>40</b>	<b>5 599 547</b>	<b>3</b>



