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RESEARCH REPORT MBL 3

AN ANALYSIS OF AUDIT COMMITTEE EFFECTIVENESS: A CASE STUDY OF PUBLIC ENTITIES IN GAUTENG

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Executive Summary

The Governance Framework in South Africa was developed through the establishment of the King Committee, led by Mervin King. This committee released its first report in 1994, known as the King Report. At the time, it was aimed at promoting the highest standards of corporate governance in South Africa.

There were major developments in the legislation and economy of South Africa after this, which prompted the revision of the King Report to King II in 2002 and King III in 2009. This revision was also coupled with the change in the Companies Act (Act No 61 of 1973), which was replaced with the new Companies Act (Act No.61 of 2008).

In contrast to the King I and II codes, King III applies to all entities, regardless of the manner and form of their incorporation or establishment, and is on an apply or explain basis. There are 29 principles documented in King III that are related to the role and functions of the board of directors. In addition, 10 principles are directed to the audit committee. State-owned enterprises are also governed by the Public Finance Management Act (Act No. 1 of 1999), as amended by Act No.29 of 1999, and the Municipal Finance Management Act (Act No. 56 of 2003). With respect to state-owned enterprises, where other acts contradict the PFMA/MFMA, the PFMA/MFMA prevails.

This study proposes that the PFMA be revised, in order to force the accounting authority to disclose material facts, including those reasonably discoverable which will influence the decisions of the executive authority, without waiting for a request from the executive authority or legislature.

The PFMA provides for the composition of the board and stipulates the minimum number of meetings per year. The Treasury Regulations provide guidelines in terms of the roles and responsibilities of the audit committee. These roles and responsibilities have been found to be in line with the

recommendations made in King III, as well as the requirements of the Companies Act.

This study focuses on the effectiveness of audit committees in public entities, specifically schedule 3A entities, which are governed by the PFMA. It is clear that the audit committee cannot operate on its own if it wishes to be effective. Management, Internal Audit and External Audit (Auditor General of South Africa) all play significant roles in the effectiveness of the audit committee. Internal Audit and the Auditor General are assurance providers for the audit committee and therefore play an even bigger role in its effectiveness. The independence of these assurance providers is vital, as the audit committee relies on them to obtain an independent view of the effectiveness of controls within the entities.

A qualitative approach is followed in this study, and selected participants are interviewed. The composition of the audit committee can be seen as a determining factor in terms of how well the audit committee exercises its oversight function. This study identifies gaps that need to be closed to ensure the effectiveness of audit committees. In addition, areas for future research are identified and recommendations are made in this regard.

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Abbreviations

King III	:	King Report on Governance for SA 2009 (King III)
PAA	:	Public Audit Act, 2004 (Act No.25 of 2004)
PFMA :		Public Finance Management Act 1999, (Act No.1 of 1999)
MFMA:		Local Government: Municipal Finance Management Act, 2003 (Act No.56 of 2003)
MSA	:	Local Government: Municipal Systems Act, 2000 (Act No.32 of 2000)
OECD	:	OECD Guidelines on Corporate Governance of State-owned Enterprises
SAA	:	South African Airways
SOX	:	Sarbanes-Oxley Act

1. ORIENTATION

1.1 Introduction

1.1.1 Background to the research topic

The Governance Framework in South Africa was developed through the establishment of the King Committee, led by Mervin King. This committee released its first report in 1994, known as the King Report. At the time, it was aimed at promoting the highest standards of corporate governance in South Africa.

Source: National Flag, www.saflag.co.za, Accessed: 22 November 2011

There were major developments in the legislation and economy of South Africa after this, prompting the revision of the King Report to King II in 2002 and King III in 2009. This revision was also coupled with a change in the Companies Act, 1973 (Act No 61 of 1973), which was replaced by the new Companies Act, 2008 (Act No.61 of 2008).

This required the establishment of a board of directors, which had a bird's eye view of the operations of the companies and entities. Because of the increasing volume of work of the board of directors, board committees, including the audit committee, were established, which consist of at least one board member who is able to report back to the full board.

The Sarbanes-Oxley Act (SOX 2002, section 2) defines an audit committee as "a committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer". A competent, committed, independent, and tough-minded audit committee has been described as "one of the most reliable guardians of the public interest" (Levitt, 2000: 5).

The Great Western Railway Company in the United Kingdom established the first audit committee as early as 1872. There was not much interest into this corporate governance until the last 10 to 15 years. This was prompted by the major corporate collapses and business failures, the issuing of various corporate governance codes and new or amendment to existing legislations. (Marx, 2009)

The audit committee meets as often as necessary, but before the board meeting, and submits reports to the full board. Audit committees need to review, among other things, the effectiveness of the internal control systems, as well as the adequacy, reliability and accuracy of the financial information provided by management.

Due to the shortage of people with financial skills and the technical know-how with regard to the internal control systems, many of the audit committee members have taken the opportunity to serve on as many audit committees as possible. This raises a question as to how effective the audit committee members are. Most of the time, management view the audit committee role as being that of rubber stamping everything it is given and then submitting it to the board for approval. Management sees no value in audit committees, which are viewed as a complete waste of time and money.

1.1.2 Purpose of the study

The purpose of this study is to explore the duties and responsibilities of the audit committee in the context of South Africa's governance framework. Audit committees, as a committee of the board of directors, exist within a governance framework, which is based on the laws, regulations, codes of best practice and policies guiding company operations. This study will analyse the effectiveness of audit committees within national public entities, with a specific focus on schedule 3A public entities.

1.2 Problem statement

The management of most public entities are of the opinion that audit committee members add little or no value to these entities. The move from King II to King III addresses certain gaps in the effectiveness of the audit committee. One of these changes is taking away the responsibility for electing the chairperson of the audit committee from the audit committee itself to the board.

A person can serve on as many audit committees as he/she wishes, and this results in insufficient time being invested in understanding each client's business and making a meaningful contribution to these clients. As a result, fraudulent activities occur and audit committee members approve documents, not knowing that they are encouraging fraud, simply because of a lack of business understanding.

1.3 Research objectives

The main objective of this study is to determine whether or not audit committees in the public sector are effective. Given the importance of the role that an audit committee plays in the governance structure of the board with regard to financial reporting, internal control and risk management, and other related aspects, and the recent developments in the legal, regulatory and business environment in South Africa, it is important to examine the effectiveness of the audit committee.

One of the questions that this study seeks to address is the following: Is the effectiveness of the audit committee measured by the independence of the internal audit, compliance by the entity of laws and regulations, or by strong internal controls and the independence of the external audit?

Based on the above, the following sub-questions can be asked

1. Does the gender composition of audit committee members influence the effectiveness of the audit committee?
2. Does the age of audit committee members influence the effectiveness of the audit committee?
3. Does the experience of audit committee members influence its effectiveness?
4. Does the independence of the internal audit influence the effectiveness of the audit committee?
5. Does the independence of the external audit influence the effectiveness of the audit committee?

1.4 Importance of the study

Marx (2009) points out that the effective functioning of audit committees in the public sector should be investigated. Given that the public sector forms an important part of the economy, it is therefore critical to investigate the effective delivery of public services. Marx argues that effective audit committees can significantly contribute to increasing the level and reliability of financial reporting and the effectiveness of internal controls and risk management systems.

There is a huge obligation on public entities to deliver on the mandate of government. Many people are complaining about service delivery and the availability of jobs, and employees are, time and again, being retrenched or suspended for a lengthy period of time. This results in job losses, and government seems to be fighting a losing battle. Government is striving towards a clean audit administration by the year 2014. All spheres of government are expected to have unmodified audit opinions, no findings with regard to pre-determined objectives and no findings of non-compliance with laws and regulations. Audit committees play a crucial role in the strengthening of internal controls, ensuring that there are synergies between assurance providers such as internal and external audits.

The achievement of the mandate of these entities and government also depends on the contributions made by the audit committee to management and the board. If the audit committee is not effective, controls may be poor, resulting in the undetected occurrence of fraudulent activities. Management can hide non-compliance with legislation and treasury regulations, and this might never be detected.

If the audit committee is ineffective, the internal audit could be undermined by management, and their findings will not be taken seriously.

In a court case in New York, the audit committee's oversight of the financial reporting process was tested, and the audit committee chair testified that he "trusted" management. Another member testified as follows: "It never occurred to him to check the truthfulness of management's statements. He always assumed that management was giving the committee a full and complete description of the affairs of the company. The audit committee put too much faith in management's integrity and continued to rely on management's assertions even after there was evidence of questionable management integrity" (Beasley, Joseph, Hermanson and Neal, 2009).

1.5 Research Design

1.5.1 Sampling procedure

There are 152 national public entities listed in the PFMA (Act No. 1 of 1999). In terms of the PFMA, each entity must have an audit committee. The population used in this study has been limited to those entities that are located in the Gauteng province. According to the database at the office of the Auditor General, there are 117 national public entities located in this abovementioned province. A sample of eight public entities was selected, which represents 6.84% of the population.

Below is a profile of the public entities that were interviewed:

Council for Geoscience (CGS)

The CGS was established in terms of the Geoscience Act (Act No. 100 of 1993). As outlined in its 2010/11 annual report, CGS's vision is to be a leader in earth science solutions, and its mission is to provide expert earth science information and services, in order to improve the management of natural resources and the environment for a better quality of life for all (Council for Geoscience, 2011).

As stipulated in the Geoscience Act, CGS is mandated to gather, compile, interpret and disseminate geoscience information for South Africa. This mandate, which is outlined in the CGS annual report, includes the following:

a) The systematic reconnaissance and documentation of the geology of the earth's surface and continental crust, including all offshore areas within the territorial boundaries of South Africa.
b) The compilation of all geoscience data and information, particularly geological, geophysical, geochemical and engineering-geological

data in the form of maps and documents, which are placed in the public domain.

c) Basic geoscience research into the nature and origin of rocks, ores, minerals, geological formations, the history and evolution of life and the formation of the earth, with a view to understanding the geological processes of both the past and present and to compile and publish such research findings nationally and internationally, in order to contribute to the understanding of the earth, its evolution and its resources.

d) The storage and preservation of all geoscience data and knowledge on South Africa in the National Geoscience Repository. This repository houses a large and growing collection of geoscience information on all the countries on the African continent. This information also includes data received from mining companies, universities and research institutions worldwide. Public access to all geoscience information is subject to existing legislation, arranged through the mandate of the Council for Geoscience.

e) The rendering of geoscience information services and advice to the State, in order to enable informed and scientifically based decisions to be made regarding the use of the earth's surface and resources, within the territory of South Africa.

f) The management of a number of national geoscience facilities on behalf of the country. These include the National Seismograph Network, an Infrasound Observatory, the National Borehole Core Repository, the National Geoscience Museum and the National Geoscience Library.

g) As part of its seismological monitoring function, the Council for Geoscience contributes to the verification of global compliance with the ban on underground, underwater and upper atmospheric nuclear explosions in terms of the Comprehensive Nuclear Test ban Treaty (CTBT), by making data available from stations located in the South African territory.

h) Provision of geoscience data and products to external clients, both nationally and internationally. These services are to be rendered on a full cost-recovery basis (Council for Geoscience, 2011: 18-19).

The CGS annual report goes on to say that CGS is in the process of compiling records of sinkholes and subsidences for a database, which will assist in the future assessment of sinkhole hazards and decision making with regard to development types and foundation designs. In South Africa, dolomite is notorious for the formation of sinkholes and subsidences.

Thousands of people reside and work in the Centurion area, which is built on dolomite and where numerous sinkholes have occurred in the past, causing significant damage to property. CGS has assisted government authorities in the field of sinkhole risk evaluation since the early 1970s, in order to ensure safe development on a foundation of dolomite. The City of Tshwane's municipality has benefited the most from this research (Council for Geoscience, 2011). This has led to the recent announcement by the Gauteng government that funding will be provided to protect and/or relocate schools in the province that are located in a dolomite area.

Film & Publication Board (FPB)

fpb
Film and Publication Board
We inform. You choose.

Source: Film and Publication Board, www.fpb.gov.za, Accessed: 19 November 2011

The Film and Publication Board (FPB) derives its mandate from the Films and Publications Act (Act 65 of 1996), which was amended in 2004 and 2009. The Act is the enabling legislative framework, and outlines the key functions, powers and duties, as conferred to the Board.

The Film and Publication Board was established in terms of the Films and Publications Act (Act No. 65 of 1996). As outlined in the 2010/2011 annual report, FPB's mandate is to regulate the creation, production, possession and distribution of films, games and certain publications, in order to do the following:

- Provide consumer advice that will enable adults to make informed viewing, reading and gaming decisions – both for themselves and for children in their care.
- Protect children from exposure to disturbing and harmful materials and from premature exposure to adult experiences.
- Make punishable the use of children in pornography or exposure thereto (Film and Publication Board, 2011).

It is the vision of this entity to be a credible and visible content regulator authority that protects consumers, and its mission is to ensure efficient and effective consumer protection through regulation of media content, while empowering the public, especially children through robust information sharing (Film and Publication Board, 2011).

According to the FPB's 2010/2011 annual report (2011: 15), "The FPB became a full member of the International Association of Internet Hotlines (INHOPE) in May 2010. This membership facilitates co-operation and partnerships with international agencies in the fight against child pornography. South Africa's hotline is the first one in Africa to receive full INHOPE membership status, and therefore has to continuously work with other African governments to ensure focus on the issue of child pornography within the continent.

During the report year, the FPB intensified its work in educating children and communities about the dangers of child pornography, exposure of children to pornographic material and other undesirable content, as well as the need to report incident of such acts when identified".

International Marketing Council (Brand South Africa)

Source: IMC, Website: www.imc.org.za , Accessed: 19 November 2011

The IMC markets South Africa, both internationally and locally. Recently, IMC changed its name to Brand South Africa – however, this name has not yet been changed in the PFMA. According to IMC's 2010/2011 annual report, it was established to lead, co-ordinate and support the creation of a positive, unifying image and to propose a national brand image for South Africa. To achieve this, the IMC collaborates with partners in the government, private sector and civil society, working together to market the country.

According to the IMC Annual Report (2011: 6), "The 2010 Brand Valuation by independent finance advisory firm Brand Finance placed South Africa at 34th overall, with a total value of US$135 billion. Further studies confirmed an improved brand reputation and image abroad".

Mine Health & Safety Council

Source: MHSC, website: www.mhsc.org.za, Accessed: 19 November 2011

MHSC monitors safety in the mines and establishes standards that mines in South Africa should adhere to. According to the MHSC (2011: 10), "The main task of the Council is to advise the Minister of Mineral Resources on occupational health and safety legislation and research outcomes focused on improving and promoting occupational health and safety in South African mines”.

According to the 2010/2011 MHSC annual report, the MHSC is established in terms of the Mine Health and Safety Act No 29 of 1996, as amended. Its board has representatives from the state, employers and labour, and the chairperson is the Chief Inspector of Mines. Its main source of revenue is from levies that are charged to mines across the country and reports submitted to Parliament through the Department of Mineral Resources.

“The council also oversees the activities of its committees; promotes a culture of health and safety in the mining industry; arranges a summit every two years to review the state of occupational health and safety at mines; and liaises with the Mining Qualifications Authority and any other statutory bodies about mining health and safety.

For the 2010/11 year, the MHSC undertook to achieve the following key measures, targets and initiatives aligned to the MHSC’s mandate of advising the Minister, promoting a health and safety culture and fulfilling compliance obligations:

- Promoting OHS [Occupational Health and Safety] culture in the sector by developing the Culture Transformation
- Compliance to the reporting framework for National Treasury and other regulatory requirements
- Advising the Minister of Mineral Resources on topical, related OHS issues
- Improving legislative aspects pertaining to OHS
- Enhancing the spirit of tripartism on which the MHSC is passed” (MHSC, 2011: 19).

National Energy Regulator of South Africa

NERSA's annual report for 2010/2011 indicates that NERSA's vision is to be a world- class leader in energy regulation, and its mission is to regulate the energy industry in accordance with government laws and policies, standards and international best practices in support of sustainable development.

The annual report further states that NERSA is a regulatory authority established as a juristic person in terms of Section 3 of the National Energy Regulator Act, 2004 (Act No. 40 of 2004). NERSA is mandated to regulate the electricity, piped-gas and petroleum pipelines industries in terms of the Electricity Regulation Act, 2006 (Act No. 4 of 2006), the Gas Act, 2001 (Act No. 48 of 2001) and the Petroleum Pipelines Act, 2003 (Act No. 60 of 2003).

In addition to the above Acts, government policies and regulations issued by the Minister of Energy inform NERSA's mandate. NERSA is expected to perform the necessary regulatory actions in anticipation of and/or in response to changing circumstances in the energy industry (NERSA Annual Report, 2011).

According to NERSA's annual report, in 2009, NERSA approved the Renewable Energy Feed-in Tariff, in order to promote investment in clean energy and to meet the country's climate change targets, as set by the government.

" The Energy Regulator contributed to the growth of the industry by registering at least ten companies engaged in production activities and importation of gas in terms of section 28 of the Gas Act, 2001 (Act No. 48 of 2001). These operations will contribute to the energy needs of certain industrial users. This process revealed the growing popularity of biogas as an alternative source of energy for rural communities and confirmed a strong pattern of new biogas projects likely to emerge in the future" (NERSA, 2011: 18).

National Film & Video Foundation (NFVF)

Source: NFVF, www.nfvf.co.za, Accessed: 20 November 2011

The NFVF's vision is "A South African film and video industry that mirrors and represents the nation, sustains commercial viability, encourages development and provides a medium through which the creative and technical talents of South Africans are able to reach the world.

Mission is to create an environment that develops and promotes the South African film and video industry domestically and internationally" (NFVF, 2010: 11).

The NFVF is governed by the NFVF Act 73 of 1997, as amended by the Cultural Laws Amendment Act 36 of 2001.

With reference to the 2010/2011 annual report, the NFVF mandate includes the following:

- To promote and develop the film and video industry
- To provide and encourage the provision of opportunities for persons, especially from disadvantaged communities to get involved in the film and video industry
- To encourage the development and distribution of local film and video products
- To support the nurturing and development of access to the film and video industry

- To address historical imbalances in the infrastructure and distribution of skills and resources in the film and video industry.

"In order to achieve these ideals the NFVF has developed the Value Charter which is the strategic interpretation of the NFVF Act. The Value Charter outlines the following mission critical strategic initiatives:

- Development of a Sectoral Information System (SIS), measure of aggregation and Key Performance Indicators (KPI's) for the film sector
- Demand stimulation and audience development
- Production of local genre and content
- Global positioning of the South African film industry
- Capital formation, infrastructure and facilities development
- Human capital development, education and training
- Establishment of the trading entity in terms of paragraph 27 of the Cultural Laws Amendment Act 36 of 2001
- The NFVF empowerment, talent incubation and funding initiative
- Intergovernmental and stakeholder relations" (NFVF, 2010: 12).

1.5.2 Data collection instruments

In this study, questionnaires will be sent to the management and audit committee members of the selected entities. Interviews will also be conducted, in order to obtain first- hand knowledge of the experiences of members of the audit committee. The questionnaires and interviews seek to identify the following:

- How the audit committee operates
- How the audit committee members are appointed
- Whether or not gender influences the audit committee in any way

- Whether or not the audit committees comply with the legislative requirements
- Whether or not the assurance (internal and external auditors) providers are independent
- What contribution is made by the assurance providers
- How management influences the effectiveness of the audit committee.

1.6 Summary

This chapter has provided a background to the study and described how this study will be conducted. The study population has been identified as schedule 3A public entities located in the Gauteng Province. This was done for logistical reasons, as it will be difficult to obtain information from other provinces. A profile of the entities that were interviewed was also provided in this chapter, as well as a description of the data collection instruments used in this study. In the next chapter, the focus will be on a detailed literature review, in order to gain an understanding of how other authors view audit committees and their effectiveness. A section of the forthcoming chapter is devoted to the Auditor General as an external audit provider mandated by the constitution, with a special emphasis on how it influences the effectiveness of the audit committee.

2. LITERATURE REVIEW

In the previous chapter, the purpose of the study, as well as the research instruments and sampling procedure, were documented in detail. This chapter will focus on the issue of corporate governance in South Africa and beyond its borders. Reference is made to the King Reports, which make considerable recommendations with regard to governance, especially at director level. The significance of this work lies in its identification of the importance of audit committees and the legislative requirements surrounding their existence. The chapter highlights the governance issues and explores the interventions that management can introduce if governance is non-existent or ineffective.

2.1 Development of corporate governance in South Africa

According to McGee (2010), corporate governance has become an important issue in transition economies in recent years. More and more directors, owners and corporate managers have begun to realise that a good corporate governance structure has many benefits. Some of the benefits of good corporate governance are an increase in share price and the ability to obtain capital more easily. One of the disadvantages of not having good corporate governance is that international investors are hesitant to lend money to or buy shares in a corporation that does not subscribe to good corporate governance principles. McGee further states that transparency, independent directors and a separate audit committee are especially important and some international investors will not seriously consider investing in a company that does not have these things in place.

The Governance Framework for South Africa was developed through the establishment of the King Committee. This committee released its first report in 1994, known as the King Report. At the time, it was aimed at promoting the highest standards of corporate governance in South Africa.

Before the King Report, the Companies Act No.61 of 1973 guided companies throughout the country. The report was essentially a guide for companies, and no one could be held liable in a court of law for not complying.

Subsequent to the release of the King Report in 1994, there were various economic and legislative developments which prompted the review of the King Report. When the report was reviewed, the second version of the report was named the King II Report. King II was released in 2002 and contained a code of corporate practices and conduct.

King II acknowledges that there is a move away from the single bottom line (that is, profit for shareholders) to a triple bottom line, which embraces the economic, environmental and social aspects of a company's activities.

In the words of the King Committee: "...successful governance in the world in the 21st century requires companies to adopt an inclusive and not exclusive approach. The company must be open to institutional activism and there must be greater emphasis on the sustainable or non-financial aspects of its performance. Boards must apply the test of fairness, accountability, responsibility and transparency to all acts or omissions and be accountable to the company but also responsive and responsible towards the company's identified stakeholders. The correct balance between conformance with governance principles and performance in an entrepreneurial market economy must be found, but this will be specific to each company."

The King Report applies to all listed companies, financial institutions and the public sector, and works on a voluntary basis, except for listed companies. The Johannesburg Stock Exchange (JSE) required all listed companies to adopt the King II Report. With the imminent changes to the Companies' Act of 1973, the King Commission also attempted to align King II with the requirements of the new Companies' Act, resulting in the King III Report. King III was published in September 2009 and came into effect on1 March 2010. "In contrast to the King I and II codes, King III applies to all entities regardless of the manner and form of incorporation or establishment" (King Committee 2009)." The Companies' Act was also revised in 2008 and was intended to come into effect on 1 July 2010. However, it finally came into effect on 1 May 2011. The new Companies' Act is known as Companies Act No.71 of 2008.

Photo: Remy Steinegger, World Economic Forum, www.mediaclubsouthafrica.com Accessed: 20 November 2011

The Companies' Act requires each company to have a board. However, the Public Finance Management Act does not necessarily require public entities to have a board, but rather to have an accounting authority. This accounting authority could be the board or the CEO. King III assumes that all public entities have a board of directors and therefore recommends that the chairperson of the board of directors is an independent, non-executive member.

Section 93J of the Municipal Systems Act (MSA) states that the board of directors of a municipal entity must appoint a chief executive officer, who is accountable to the board of directors for the management of the municipal entity. In addition, the MFMA, in section 93, indicates that the chief executive officer is the accounting officer. This is in contrast to the PFMA, which clearly makes the board of directors the accounting authority (equivalent to the accounting officer in the MFMA). If the entity does not have a board, the chief executive officer is then the accounting authority.

An emphasis on audit committees has been placed mainly by audit committees of private companies, and a lot of gaps have been identified and improvements made following the collapse of many companies. Corrigan (2009) highlights gaps such as audit committee agendas and information flow as areas that need attention. He also alludes to the fact that audit committee members are not visiting company's foreign operations to get an understanding of what is going on there. The increase in the focus on risk management by private company audit committees is commendable - however, the question remains as to whether or not these changes are being filtered through to the audit committees in schedule 3 public sector entities.

2.2 Overview of public entities

There are three spheres of government, namely national, provincial and local. In all these three spheres, public entities exist. The aim of public entities is, among other things, to assist government to fast-track its delivery of services and economic growth. As an example, South African Airways is one of the public entities in the national sphere of government. It operates on a commercial basis and is able to effectively increase employment, thereby stimulating economic growth. The Department of Public Enterprise is the sole shareholder of this public entity. Another example is City Power, a public entity that falls under the local sphere of government - it is also operated on a commercial basis and provides electricity to the residents and businesses in the Johannesburg Metro. The Gauteng Tourism Authority aims to promote tourism only in the Gauteng province - it is not operated on a commercial basis and is fully funded by the provincial government.

A schedule of all public entities in the national and provincial sphere can be found in the Public Finance Management Act. All major public entities are listed in Schedule 2 of the PFMA and include, among others, ESKOM, South Africa Nuclear Energy Corporation, South Africa Broadcasting

Corporation, etc. National public entities are listed under schedule 3A of the PFMA and include, among others, the Film and Publication Board and National Energy Regulator of South Africa.

National government business enterprises are listed under schedule 3B of the PFMA and include, among others, the Council for Mineral Technology (MINTEK), Council for Scientific and Industrial Research (CSIR), etc. Provincial public entities are listed under schedule 3C of the PFMA and include, among others, Eastern Cape Parks Board, KwaZulu-Natal Gambling Board, Limpopo Development Enterprise, etc. Provincial government business enterprises are listed under schedule 3D of the PFMA and include, among others, the Free State Development Corporation, Ithala Development Finance Corporation and Mafikeng Industrial Development Zone (Pty) Ltd.

Public entities operating in the local sphere of government are governed by the MFMA. Unlike the PFMA, the list of public entities is not available in a schedule of the MFMA. Each municipality maintains its own record of the municipal entities under its control.

2.3 Issues faced by public entities

Each public entity is established through a mandate either from an enabling legislation or by a shareholder compact, or even through a budgeting process. The entities need to perform and achieve the objectives identified by the founding department or municipality. When the mandate is not being achieved, the executive authority can close that public entity. An example is the recent closure of the Electricity Distribution Industry Holdings (Pty) Ltd, a public entity falling under the Department of Energy. This entity was established with a mandate to develop Regional Electricity Distribution (REDs) in the country within 5 years, starting in 2004 (EDI Holdings, 2010). This mandate was not achieved over a period of 7 years and in 2010, the Minister recommended to parliament and the cabinet made its final decision in December that year to close the entity down as from 1 April 2011. One of the responsibilities of the audit committee in the PFMA is to review the risk areas of the institution's operations. One may ask a question as to how effective the audit committee has been in ensuring that the mandate of the aforementioned entity is achieved.

"At no time in recent memory is the need for an effective audit committee in government more important than now. With looming budget shortfalls, program cuts and employee layoffs, government units are wrestling with maintaining services with fewer resources. Government officials need to diligently assess the need for expenditures and ensure that revenues are received timely and managed correctly. There is simply no room for inefficiency or waste when these government units are faced with making difficult decisions about program cuts." (Shulman and Tim, 2011:1)

Photo: Remy Steinegger, World Economic Forum, www.mediaclubsouthafrica.com Accessed: 20 November 2011

2.4 Duties and Responsibilities of Directors

The primary duties of the board of directors, as highlighted in the Companies Act and common law, are to act honestly and lawfully, and to exercise care, skill and diligence. According to Naidoo (2009: 162), "the highest legal duty of the board of directors is to act honestly, in good faith and in the best interest of the company". Similarities can be found between the Companies Act and PFMA.

The PFMA and the MFMA require the accounting authority or officer for a public or municipal entity to do the following:

(a) exercise the duty of utmost care to ensure reasonable protection of the assets and records of the public entity;

(b) act with fidelity, honesty, integrity and in the best interests of the public entity in managing the financial affairs of that entity;

(c) on request, disclose to the executive authority responsible for that public entity or the legislature to which the public entity is accountable all material facts, including those reasonably discoverable, which may in any way influence the decision or actions of the executive authority or that legislature; and

(d) attempt, within the sphere of influence of that accounting authority, to prevent any prejudice to the financial interests of the state.

With respect to (c) above, unlike the PFMA, the MFMA does not require the accounting officer to wait for a request - the accounting officer must disclose to the entity's parent municipality and the entity's board of directors any material facts.

According to Naidoo (2009), good corporate governance practice requires all companies to be lead by a board that should "direct, govern and be in effective control of the company" (King III, 2009). In addition, the board should ensure the accountability of the company to all its stakeholders. Naidoo (2009) provides the example of the SABC board, in that, added to its responsibilities in terms of the SABC's founding legislation, South African company law and codes of governance such as the King Reports, directors of state-owned entities have personal accountability for the integrity and efficacy of financial controls in terms of the PFMA.

2.5 Duty of proper purpose

This duty requires directors to only use their powers for the purpose for which those powers were conferred, and not for any unauthorised or collateral purposes (Naidoo, 2009). One of the purposes is to appoint the CEO of the company and establish a framework for the delegation of authority.

2.6 Duty of good faith

According to Naidoo (2009: 164), a director must exercise good faith, honesty and integrity in all dealings with or on behalf of the company. The King Report's principles require the board and its directors to act in the best interests of the company, and this is echoed by the Companies Act. When a director does not act in good faith, he/she may be held liable by the company. As an example the directors of Enron were not acting in good faith and were therefore held liable for the collapse of Enron.

2.7 Independence of action

Directors are required to act independently in executing their responsibilities. The King Report stresses the importance of independence, to the extent that the majority of non-executive directors should be non-executive. "SAA has a unitary Board comprising 13 non‐executive directors and 2 executive directors. All non‐executive directors are appointed by the Minister of Public Enterprises". (SAA annual report 2010: 31) It is, however, not clear whether or not the chairperson of the board is an independent non-executive member.

2.8 Duty of care, skill and diligence

Each director is expected to execute his/her responsibilities with care, skill and diligence. This responsibility can be compromised when a director is holding too many directorial positions in companies. Hence, King III recommends, in one of its directives, that any chairman or director should carefully consider the number of other chairmanships he holds.

A director may not be able to exercise this responsibility if he does not get the information for meetings in time and/or takes time to understand the business of the company. Most of the time, agendas for directors' meetings are prepared by management, and not necessarily by the board.

Directors at South African Airways approved a framework whereby the CEO could give retention bonuses to staff. The CEO was taken to court by SAA for overpayment of bonuses to a value of R24.7 million (Basson and Gedye, 2010).

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“In exercising their duty of care, directors should ensure that prudent steps are taken to ensure the integrity of the company’s information and IT systems. IT risk should be specifically dealt with by the risk committee (or the audit committee in the absence of a risk committee) and regular reports on disaster recovery plans, data security and the integrity of IT systems should be presented to and noted by the board” (Naidoo 2009: 279).

“In exercising their duty of care the directors should ensure that prudent and reasonable steps have been taken in regard to IT governance. IT governance should focus on:

- Strategic alignment with performance and sustainability objectives of the company;
- Development and implementation of an IT governance framework;
- Value delivery: concentrating on optimising expenditure and proving the value of IT;
- Risk management: addressing the safeguarding of IT assets, disaster recovery and continuity of operations; and
- The protection and management of information (PriceWaterhouseCoopers. 2009:4)”.

2.9 Duty to act intra vires

Naidoo (2009) states that directors are agents of the company and they may act only within the scope of their authority, both express and implied (intra vires or within the powers). Most companies are guided by the memorandum of incorporation, which may limit the powers of directors. When a director has exceeded his powers, he may be held liable by the company or such an act may be ratified by the board. Ratification does not mean that the company/ entity will leave those directors who acted outside their powers alone. The company may claim damages from directors for losses suffered. It can be argued that the former CEO of SAA has acted outside the scope of his powers in approving tenders in which he had an interest. In the public sector, this is not enforced for the most part- one may therefore argue that it is swept under the carpet.

2.10 Acts which cannot be ratified

There are acts by directors that cannot be ratified - these include acts that are in contravention of the Companies Act. A director may act in good faith and for the benefit of the company, but if such an act is in contravention of the Companies Act, the company cannot ratify it. A shareholder, director, officer or trade union may then bring legal action against the company to prevent it from committing an act which is in contravention of the Act or memorandum of incorporation (Naidoo, 2009).

2.11 Liability to account for profits

Each director should disclose all profits made during his/her directorship. The director may not use his knowledge as a director and then get a contract and resign from his position. He is liable to the company to disclose such information, and if the company has suffered any loss as a result of the action by the director / former director, it can claim this from him/her to the extent of the profits made by the director or former director.

In the case of *SAA vs Ngqula*, “the forensic investigation has raised questions about a jet fuel tender that was awarded to a company in which Ngqula allegedly has an indirect interest. KPMG further found the awarding of a tender for in-flight catering was irregular.” The PFMA defines irregular expenditure as that incurred in contravention of an act. “The tender was awarded to French catering group Servair, but questions were raised about the group's local partner, run by Vusi Sithole, an associate of Ngqula and a business partner of his wife.” (Basson and

Gedye, 2010:12). The former CEO should have disclosed this interest before the tender was awarded.

2.12 Duty to act "as a board"

Directors are expected to work in unity or as a collective. Decisions made at board meetings are the decisions of the board, not individual directors. When a board member disagrees with the decision, a director is at liberty to ask the company secretary to minute his disagreement. This will protect the director in case a liability arises.

Naidoo (2009) goes a step further and introduces the public sector perspective, combining it with the King Report recommendations. Naidoo 2009 states that the King Report recommends that the board adopts a charter in which it outlines its responsibilities in relation to management. In addition, the Protocol recommends that each board has a performance agreement which clearly states how its performance will be monitored and assessed. Naidoo (2009) further states that the Protocol suggests that the role of the shareholder in decision making by the board should be agreed on and clearly defined in a shareholder compact between the state and the organisation.

2.13 Sustainability as a business opportunity

The board members are required to look after the company and ensure that it is sustainable. SABC was involved in a crisis that required it to be bailed out by government. This happened when the chairperson was Khanyi Mkhonza. During Ms Mkonza's short tenure, the SABC lost the Premier Soccer League broadcast rights and now needed a R2-billion bailout to keep it afloat. The board also failed to stem the tide of experienced journalists leaving the broadcaster (Groenwald and Mataboge, 2009).

The Mail and Guardian *M&G* reported that Andile Mbeki was the first board member to ask Mkhonza to resign when the board members were dissatisfied with her hiring a car and a driver at a cost of R200 000. This expenditure was because she did not have a driving licence. In addition to the R200 000, she also spent R180 000 on a security guard posted outside her home (Groenwald and Mataboge, 2009).

Naidoo (2009) acknowledges the importance of sustainability reporting, making reference to King III, which draws specific attention to sustainability reporting. Naidoo (2009) stresses that the days of the annual report focusing on financial performance with a small section on social, health and environmental issues are now over. Companies are now required to publish an integrated report focusing equally on financial, governance, strategy and sustainability issues. The picture presented should be of the true economic value of the company as an entity, not just a snapshot of its financial value.

2.14 Board committees

In order for the board to perform its responsibilities effectively, it needs to delegate certain functions to its board committee. These committees include the following:

- Audit committee
- Risk committee
- Remuneration committee.

The above committees help the board to ensure that the company or entity has and maintains an effective, efficient and transparent system of financial and risk management and internal control. The assurance providers, such as internal audit and external audit, should operate effectively. According to King III, the board should delegate certain functions to well-structured committees, without abdicating its own responsibility. The chairperson of the audit committee, in the case of a company, needs to be an independent non-executive who is appointed by the shareholders. In many entities and the private sector, the audit committee and risk committee are combined into one committee, which is usually known as the audit and risk committee. In this study, the term 'audit committee' refers to this combined committee.

2.15 Audit Committee

According to Kana (2010), an independent audit committee fulfils a pivotal role in corporate governance. It is important to, *inter alia*, ensure the integrity of integrated reporting and internal financial controls, and to identify and manage financial risks. In order to carry out their mandate to the full extent, audit committees should be suitably skilled and qualified to deal with their responsibilities of overseeing integrated reporting and co-ordinating the activities of the various assurance providers.

Shulman and Tim agree with Kana (2010), and describe the role of the audit committee as that of offering an independent view of the government unit. They state that it is not constrained by day-to-day concerns with which unit managers are faced, but rather that it is responsible for keeping the government unit focused on identifying and mitigating risks, ensuring accountability and compliance, and establishing a governance structure.

The King III recommends the following principles for the audit committee:

a) The board should ensure that the company has an effective and independent audit committee;
b) Audit committee members should be suitably skilled and experienced, independent, non-executive directors;

In regard to the above, Shulman and Tim (2011: 2) state that "The audit committee should be made up of members that have a level of financial and programmatic knowledge to read and understand audit reports and comprehend the associated risks identified”

c) The audit committee should be chaired by an independent non-executive director;

d) The audit committee should oversee integrated reporting;

e) The audit committee should ensure that a combined assurance model is applied, in order to provide a coordinated approach to all assurance activities;

f) The audit committee should satisfy itself of the expertise, resources and experience of the company’s finance function;

g) The audit committee should be responsible for the overseeing of internal audit;

h) The audit committee should be an integral component of the risk management process;

“The audit committee ... is responsible for keeping the government unit focusing on identifying and mitigating risks, ensuring accountability and compliance, and establishing a governance structure.” (Shulman and Tim, 2011:2)

i) The audit committee is responsible for recommending the appointment of the external auditor and overseeing the external audit process;

“In this role, the audit committee is responsible for hiring the internal and external auditors and overseeing the government unit’s overall control environment, governance and management processes. Government unit managers are responsible for their subordinates, while the audit committee is responsible for the managers” (Shulman and Tim, 2011:1).

In contrast to the above, the PFMA is silent on the recommendation by the audit committee to appoint external auditors. This is due to the fact that the PAA, read together with section 188 of the Constitution of the Republic of South Africa (Act No. 108 of 1996), provides for the Auditor-General as the external auditor in all spheres of government.

j) The audit committee should report back to the board and shareholders as to how it has discharged its duties.

The above principles are in line with the requirements of the PFMA and Treasury Regulations. However, the Treasury Regulations go a step further by stating that “the relevant executive authority must concur with any premature termination of services of a member of the audit committee” (TR 27.1.5).

An audit committee can only be effective if it has the right characteristics. Thus, the value of an effective audit committee hinges on the characteristics it possesses. This was described as follows by English, who conducted research on audit committees in Australia in the early 1990s: “the value of an audit committee is directly related to the calibre of its members, its status in the eyes of the board and senior management and its charter” (English, 1994). Audit committees can also only be effective if the audit committee members themselves, as well as all the parties the committee interacts with, clearly understand and respect the committee’s rights, duties and responsibilities. Only then will there be honest, open and constructive dialogue and interaction between the relevant parties and the audit committee” (Marx, 2009:15).

The *Accountancy Magazine* of June 2009 showed the importance of the audit committee in the corporate governance regime, indicating that it was important in building market trust (Croner CCH Group Limited, 2009).

Gauthier (2007) agrees with some of the authors, suggesting that the audit committee is responsible for selecting the independent auditor, as well as providing independent oversight and a public report on its performance. However, in all spheres of government, the responsibility for selecting an independent auditor is not that of the audit committee. The Public Audit

Act (PAA) clearly states that a government institution must be audited by the Auditor-General. If the Auditor-General is unable to perform an audit, he may choose to appoint an audit firm to perform the audit on his behalf.

SueRedman (2009) points out that there is no ‘one size fits all’ in terms of providing information to audit committee members. She further suggests that the chair of the audit committee needs to inform “each committee member as to how he or she would prefer to receive and review information and then customize this information accordingly”. This will save time by focusing on relevant information that will assist committee members to deliver on their fiduciary responsibilities.

Audit committee documents or packages, should be guided by the audit committee charter, which assists audit committee members with the roles and responsibilities. The timing of the review of these documents will also be guided by the quarterly requirements of the entity. Treasury regulations require public entities to submit, on a quarterly basis, the financial performance of the entity and the performance against pre-determined objectives. These quarterly reports will then form part of the audit committee packages.

Ward (2009) indicates that before the introduction of SOX, the audit committee charter was less than a page, and since SOX was introduced, it has now grown to more than six pages. This resulted in more work for the audit committees. In light of this, the King III report suggests that the director should consider the number of directorial positions that he/she is holding.

“Under The Sarbanes-Oxley Act, Section 407, a company is required to annually disclose whether it has at least one "audit committee financial expert" on its audit committee and, if so, the name of the expert [and] whether the expert is independent of management.

The U.S. Securities and Exchange Commission rules define the term "audit committee financial expert." This expert should:

1. Understand financial statements and generally accepted accounting principles;
2. Be able to assess their application in connection with accounting for estimates, accruals and reserves;
3. Have experience "preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are that are comparable in scope and complexity to those of the company,"
4. Be familiar with internal controls and financial reporting procedures; and
5. Understand the audit committee functions". (Ward, 2009:30).

In contrast to other countries such as South Africa, "there are no specific regulatory or legislative requirements for establishing audit committees in the New Zealand public sector"(Magrane and Malthus, 2010:427). The audit committees that exist are being criticised for their lack of expertise and experience. It is, however, encouraging to see that the Auditor-General of New Zealand is providing guidelines and best practice for audit committees in that country.

"The importance of strong governance and internal controls within public sector entities such as DHBs was brought to the fore recently when the largest fraud in New Zealand public sector history occurred at the Otago DHB in 2008 (Peart, 2008). Over a six year period a former chief information officer (CIO) at the DHB and an outside accomplice invoiced for non-existent maintenance and computer program updates, amounting to NZ$16.9 million. The fraud, which went unnoticed by the DHB's audit committee and its internal and external auditors, led to the conviction of the CIO and his accomplice, and the sacking of the chairman of the board" (Hartley, 2008)" (Cited in Magrane and Malthus, 2010:428).

In a study of the Malaysian market, conducted by Bliss et.al (2007), it was found that where the board is dominated by the CEO, it is very likely that audit fees will be high because of the perceived risk by external auditors.

In a study conducted by Mustafa and Youssef, it was found that an independent AC member is only effective in reducing the occurrence of misappropriation of assets in publicly held companies if he/she is also a financial expert.

According to the Treasury Regulations, the audit committee must meet once a year with external auditors (Auditor-General). In this meeting, the parties will discuss and resolve any outstanding issues of concern. Although this regulation does not necessarily state that this meeting should be without management, it is clearly understood in practice that the intention of Treasury is for a separate meeting without management to be held.

With reference to the qualifications of the audit committee, King III recommends that "the audit committee as a whole should have a good understanding of:

- Integrated reporting, including financial reporting and sustainability issues
- Internal financial controls
- Internal and external audit processes
- Corporate law and risk management
- IT governance as it relates to integrated reporting
- The governance processes within the company." (KPMG, 2009:9).

A practical example of the failure by the board is documented by Naidoo (2009). This example relates to the collapse of LeisureNet, whereby the former LeisureNet group non-executive chairman, Joe Pamensky, a chartered accountant and director of several high-profile companies, told the Commission of Inquiry that although he was aware of important information kept out of financial reports to shareholders before the group's collapse, for 'practical reasons' the final responsibility for the integrity of the company's financial reports had been devolved to a subcommittee of the board's audit committee. The chairman indicated that this was done because each of the directors had his or her own area of expertise and not many of the directors had the requisite knowledge and expertise 'to deal with the refinements of audited financial statement'. Interestingly enough, LeisureNet's audit committee had no less than six chartered accountants.

Naidoo (2009) argues that while there is no problem with the course of action followed by the board of LeisureNet in delegating the fine examination of the company's financial statements to a subcommittee of its audit committee, the board as a whole remained fully accountable for their approval. "In order to comply with its statutory duties, the subcommittee's report on the financials should have been presented to the audit committee and, in turn, to the full board for approval" (Naidoo, 2009: 144).

The internal audit function provides the audit committee with a means of monitoring and evaluating whether or not controls put in place within the organisation are adequate, functioning effectively and sufficient to address risks in the financial reporting process and risks in achieving strategic objectives (performance information). Internal audit typically reviews business processes and associated controls, operational and financial performance, compliance framework, IT risk and controls, and the safeguarding of assets within the organisation

The audit committee responsibilities with reference to King III now require it to focus on sustainability reporting. "Sustainability reporting should be focused on substance over form and should transparently disclose information that is material, relevant, accessible, understandable and comparable with past performance of the company" (King III, 2009:103).

King III also suggests that companies could utilise international and local guidance materials in developing and improving their stakeholder identification and engagement.

2.16 Importance of the role played by external audits

An external audit is performed by independent audit firms in the private sector. All companies established in terms of the Companies Act are subject to an audit - this requirement excludes non-profit organisations and close corporations. In the case of the public sector, all entities in which public funds are utilised are subject to an audit by the Auditor-General.

In performing this role, the Auditor General supports the audit committee in its oversight role. The Auditor-General, in its mission statement, indicated that it exists to strengthen the country's democracy by enabling oversight, accountability and governance in the public sector (Auditor General South Africa, 2011).

The Deputy Auditor General (DAG), Tembekile Makwethu, indicated in the annual report of the Auditor General South Africa that IRBA performed a firm-level review during 2010/11. This was done to determine whether or not AGSA complied with the requirements of International Standard on Quality Control (ISQC1), and the results were such that the AGSA did not only comply with the ISQC1 for audit institutions, but also its internal monitoring processes (Auditor General South Africa, 2011).

The above highlights the responsibility that the AGSA has given itself to ensure that it supports audit committees and all those charged with the governance of the entities. It is interesting to note that the AGSA has, as part of its strategic objectives, clarified its understanding of stakeholders' needs by providing for the simplicity, clarity and relevance of audit messages.

“To build public confidence and assist in improving the way national governmental system work, we must ensure that we deliver audit reports that clearly establish the status quo of the financial and performance management in the public institutions and entities... Presenting the results in clear and understandable language aids the acceptance of those results by the general public and those charged with governance and where appropriate enables the authorities to pursue further actions.

In 2010-11...the emphasis was placed on reporting against pre-determined objectives which necessitated measuring the performance results and improving service delivery. As a result, there was increased awareness and a commitment to improve the quality of the planning processes within the government. ...we reported on the assessment of compliance with laws and regulations, focusing on supply chain management, procurement processes, weak controls management and irregular expenditure. We intend following through on these fundamental risks in the next cycle in line with the commitments made by the executive and oversight to effect sustainable change in the public sector environment” (Auditor General South Africa, 2011: 13 – 14).

2.17 Summary

The time when a person could be a board member in too many companies are over. There are a lot of risks that a director faces in being a board member. South Africa, like OECD member countries, is making strides towards being in the forefront on corporate governance issues.

A good example was set by South African companies, especially banks, during the recession of the last two years. Board members were able to understand the developments leading up to the recession and managed to act in the best interests of the company, in order to save companies from going under. Many companies abroad had to be bailed out by their governments - for example, Chrylser and General Motors in the United States of America.

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The board of directors should act as the focal point of corporate governance. Many of the mishaps in SAA could have been avoided if the board had had a closer look at the finances.

King III requires that the board and management of any company, regardless of its size, should be fully committed to the goal of supporting and maintaining an effective audit committee:

1. Responsibility of the audit committee has been extended beyond financial reporting to include sustainability reporting;
2. The constitution, size and sufficiency and appropriateness of the skills set of the audit committee may need to be reconsidered by the board ;
3. An assessment of in-house skills and the qualifications/track record of external assurance providers should be performed;
4. Audit committees are to coordinate the utilisation of appropriate assurance providers in the assurance model to provide assurance on the identified risks;
5. Increased time and resource commitments are needed for audit committees, management and internal audit to

adequately review internal financial controls (PriceWaterhouseCoopers, 2010).

The audit committee is one of those committees that King III specifically mentions. However, the concept of an audit committee is not a new one, since it exists in King II and is also required by the Companies Act (1973) for certain companies. However, the additional responsibilities imposed on the committee by King III and the Companies Act (2008) highlight the importance of the committee from a corporate governance perspective.

The next chapter focuses on the methodology used in this study. It differentiates between qualitative and quantitative research methods and looks at various models in terms of their relevance to the study.

3. RESEARCH METHODOLOGY

3.1. Introduction

The previous chapter provided a comprehensive background to the literature applicable to this study. The focus now shifts to the methodology used in this study and what techniques were applied. It is important to note that various authors have different preferences with regard to the techniques and models that are applied in research. Relevant models and techniques were chosen for this study and ethical considerations are also discussed in this chapter.

The objective of this study is to find out whether or not audit committees in the public sector are effective. Given the important role that an audit committee plays in the governance structure of the board with regard to financial reporting, control and risk management and other related aspects, and the recent developments in the legal, regulatory and business environment in South Africa, this study seeks to determine whether or not current audit committee practices are effective.

3.2. Overview of research methods

“Quantitative research involves looking at amounts, or quantities, of one or more variables of interests (Leedy and Ormrod, 2010:94).” Qualitative research, on the other hand, allows the researcher to identify cause and effect relationships. It provides answers to questions such as: Why did that happen? What is the root cause of ABC? (Leedy and Ormrod, 2010).

According to Lee (1999), there is a friction between qualitative and quantitative traditions because there are no specific and agreed-upon definitions of what constitutes qualitative and quantitative research. Lee also indicates that Creswell (1994) identified five differences between qualitative and quantitative research, while Cassell and Symon (1994) identified six differences.

Leedy and Ormrod (2010) assert that qualitative research encompasses several approaches to research that are, in some respects, quite different from one another. However, all qualitative approaches have two things in common. Firstly, they focus on phenomena that occur in natural settings – to be exact, in the "real world." Secondly, they involve studying those phenomena in all their complexity. Basically, qualitative research provides means "through which a researcher can judge the effectiveness of particular policies, practices, or innovations" (Leedy and Ormrod, 2010).

Based on the above description, a suitable method for this study is qualitative research. According to Leedy and Ormrod (2010), there are five common qualitative research designs: (a) Case study, (b) Ethnography, (c) Phenomenological study, (d) Grounded theory study and (e) Content analysis. Leedy and Ormrod describe these as follows:

a) Case study: This is an in-depth study of a particular individual, programme or event for a specified period of time. Such a study may be conducted, for example, in the treatment of HIV.

b) Ethnography: Unlike a case study, where the focus is on an individual or event, ethnography looks at an entire group over a period of several months or years. The group should, however, share common characteristics, e.g. rituals or language.

c) Phenomenological study: "…is a study that attempts to understand people's perceptions, perspectives and understandings of a particular situation….what is like to experience such and such?" (Leedy and Ormrod, 2010: 141).

d) Grounded theory study: This uses data to develop theory. The ultimate goal of this research design it is to develop a theory about what the study focuses on.

e) Content analysis: This is a detailed systematic examination of the contents of a particular body of material for the purpose of identifying patterns, themes or biases.

Of the above designs, the most relevant one is the phenomenological study. This is chosen for this study because audit committee attendees will be providing qualitative information in terms of their perceptions, perspectives and understanding of the effectiveness of audit committees in the public sector.

The units of analysis are the frequent attendees of audit committees of national public entities in the Gauteng province, as well as audit committee members and management. Data was collected using questionnaires addressed to the management, frequent attendees and audit committee members.

3.3. Ethical considerations

Ethical issues were considered as part of the research, and included the confidentiality of information obtained during the interviews and returning of documents from the auditees, such as audit committee minutes. A formal correspondence requesting permission to conduct the research was sent to the chief executive officers of the selected entities (see Appendix B). This correspondence also detailed the ethical considerations that applied to this study.

3.3.1. Protection from Harm

The participants such as management and internal and external auditors, who may have been dissatisfied and therefore disengaged from a relationship with the audit committee, may have been biased and exaggerated opinions with regard to their perception of the audit committee, due to the physiological discomfort of having to recall the reasons for their defection and to honestly express their feelings and perceptions about the audit committee.

The audit committee members may feel uncomfortable, as the interviews involve the very people with whom they sit around the table, and they would like to protect their jobs as audit committee members.

In all the above cases, the confidentiality of the sessions was emphasised and an assurance of the good intentions of the study was given at the start in a less interrogative and more collaborative and participative manner.

3.3.2. Informed Consent

The full participation of all audit committee attendees cannot be completely guaranteed, despite advising them that the information they provide is confidential. However, it would also not be fair to withhold information regarding the objective of the study (poses ethical problems!), even if the aim is to ensure maximum participation and feedback. The latter is really a subjective and perception issue, which may be influenced by how the audit committee attendees have been involved with the said audit committee.

3.3.3. Right to Privacy

This study has withheld the names of the participants who may have compromising information which could influence any future deliberations and decisions of the audit committee. The results of the study have been documented in such a way that all entities that participated in the study are protected.

3.3.4. Professional Codes of Conduct

This study has abided by the code of ethics of relevant entities participating in the study. This has been performed with due consideration of the legal and confidentiality implications, while seeking innovative engagement with identified participants, in order to help improve the effectiveness of audit committees in the public sector.

3.4. Budgetary Constraints

Due to budgetary constraints, unpaid volunteers will be used.

3.5. Sampling procedure

There are 152 national public entities listed in the PFMA (Act No.1 of 1999). In terms of the PFMA, each entity must have an audit committee. The population has been limited to those entities located in the Gauteng province. There are 117 national public entities located in the Gauteng province, and a sample of eight public entities was selected, which represents 6.84% of the population.

The audit committees are predominantly constituted by a minimum of three independent non-executive audit committee members. Attendees of the audit committee include at least one representative from management, one from internal audit and one from external audit. It is expected that at any given time, there should be at least five attendees in the meeting, resulting in a sample of 40 audit committee attendees.

3.6. Research instrument

A conversational interview technique was used to collect data. This technique, simply put, is two individuals casually chatting about a given topic at a specific point in time (Lee, 1999). The data collection instrument, in the form of a questionnaire, comprised structured and open-ended questions, and was sent to respondents and followed up with telephonic and personal interviews. Personal interviews were held with the chairpersons of the audit committees, CFOs and external auditors of the selected entities.

The interviews were exploratory and unstructured, with the aim of testing the compliance with various legislations and use of guidelines provided, such as the King Code on corporate governance.

To ensure that the interview was successful, the following was provided to the interviewee: a) The purpose of the interview; b) An overview of the agenda; c) The fact that the interview process would include note- taking and tape recording.

Background variables

The background variables in this study are gender, age and years of employment. Gender is a qualitative categorical variable that divides the respondents into either “female” or “male” groups. The analysis of data for this variable is therefore limited, since this variable can only assume either a “female” or “male” value. In addition, the gender categories have names but no numeric order. Therefore, the measurement level for the gender variable is nominal.

The variables of age and years of employment are essentially quantitative, continuous variables, because they can assume decimals or fractions (e.g. 3 years, 6.5 years). In addition, the two variables have an absolute zero characteristic, i.e. regardless of the unit of measure used, relative comparisons can be made. Therefore, the measurement level for these variables is essentially a ratio scale. These variables are classified as qualitative discreet variables, and their measurement level is ordinal.

3.7. Data Analysis

3.7.1. Procedure

Thomas (1999) identifies five modes of analysing interview data. These modes are as follows: meaning condensation, meaning categorisation, narrative structuring, hermeneutic meaning interpretation, and ad hoc methods.

According to Thomas (1999), meaning condensation involves the reduction of data, at the same time articulating the data’s most important themes, whereas meaning categorisation distributes statements from the interview data into quantifiable categories.
“Narrative structure seeks to identify and reconstruct the interview text into longer stories”, while “Hermeneutic meaning interpretation requires that the researcher impose meaning based on the perspectives from a pre-existing paradigm (Thomas, 1999: 92-93)”.

The interviews conducted in this study were analysed using the meaning condensation mode. At first, all interview notes were read and then analysed individually. During the analysis, themes were identified and portions of the interview were condensed and allocated to the identified themes. The themes were then linked back to the study's research question and "integrated into a coherent and non-redundant structure" (Thomas, 1999: 91).

3.7.2. Limitations

In determining the population, the entities considered are those listed in the PFMA - subsidiaries that may fall under those entities have not been considered, as these are unknown. The total population may include dormant companies, as the PFMA does not distinguish between active and inactive entities. The sample selected was eight entities, of which only six managed to give approval for the research to be conducted within the time frame for concluding the research. The sample used was therefore reduced from 6.8% to 5.13%.

3.8. Conclusion

This chapter presented a comparison between qualitative and quantitative research. Reasons were provided as to why qualitative research is most suitable for this study and which technique was used to interrogate the data. The following chapter will focus on the actual outcomes of the research and demonstrate how the research objective was achieved.

4. RESEARCH RESULTS

The previous chapter discussed the research methodology that was used in the study. In this chapter, the results of the research are documented. A profile of all the respondents is given and no names are used, in order to ensure confidentiality.

The respondents included:

- CEOs of the entities, who are in charge of the operational effectiveness of the public entities, in terms of the PFMA;
- Chief financial officers of the entities, who are responsible for providing financial information to the audit committees on a quarterly basis;
- The chairpersons of the audit committee who are responsible for the oversight of the entities and report directly to the board, which is the accounting authority for the entities in terms of the PFMA;
- The engagement managers from the external auditors (Auditor-General), who specialise in the auditing of the public sector; and
- Internal auditors, who provide the audit committees with reports on a quarterly basis with regard to the effectiveness of internal controls.

Respondents agreed that the primary objective of the audit committee is to interrogate management reports and actions, as well as to provide assurance to the board that risks are managed and finances are in order, and that the entity is likely to achieve its objectives. In addition, it provides assurance with regard to the integrity of the financial statements and related disclosures, and oversees integrated reporting.

Respondents agreed that the age and gender of the audit committee members have no impact on the effectiveness of the audit committee. What is more important is the relevant work experience and skills to execute the responsibilities of the audit committee, as determined from time to time. The number of years of work experience was also considered to be unimportant, to an extent that it is not relevant to the roles and responsibilities of the audit committee.

4.1 Composition of the audit committee

Audit committee members emphasised the importance of the skills that the committee possesses. Predominantly, skills were required for a financial person - however, it is clear from the research that the skills required are not only financial. There should be a complementary understanding of the laws and regulations governing the public entities. Experience in the public sector is one of the questions asked during the interview of audit committee members, as the entities only work in the public sector, which is governed differently to the private sector.

All the respondents agreed that the composition (technical, IT, financial and governance experience) of the committee is very important for the effectiveness of the audit committee. Some even argued that the skills set within the committee enable it to ask the right questions.

There is a common understanding that continuing education for audit committee members, both formal and informal, is also important. This ensures that the members keep abreast of changes in accounting, legislation, relevant disciplines and new trends. Leading committees are creating a more integrated approach to training by clearly articulating, at the beginning of the year, the topics and time that the committee will devote to continuing education, even incorporating selected topics into meeting agendas.

This refers to the grouping of committee itself. The committee includes non-executive members, of which the majority are independent non-executive members. As discussed in the literature review, the PFMA requires that the audit committee has at least three members. It was noted that all entities selected in the sample for this study complied with this requirement.

The focus of the PFMA and Treasury Regulations is more on the financial people - as such, Treasury Regulations require that the majority of persons serving on an audit committee are financially literate. This poses a challenge for many of the other areas such as IT, because most of the audit committees do not have skilled IT members. The King III closes this gap by referring to suitably skilled and experienced directors. Now that the King III also applies to state-owned companies, this issue should receive a lot of attention in the public sector.
It was interesting to note that all the audit committees are led by independent non-executive members. This fulfils the Treasury Regulations requirement, as well as that of King III.

4.2 Continuation of professional education

As this theme suggests, the audit committee members cannot remain on the educational and skill level that they were when they qualified. One audit committee member at NERSA said: ‘Continuing education, both formal and informal, for audit committee members is also important. Leading committees are creating a more integrated approach to training by clearly articulating at the start of the year the topics and time the committee will devote to continuing education, even incorporating selected topics into meeting agendas.’ What the member said is in line with King III, which states that audit committee members should keep themselves up to date with key developments in financial reporting, as well as relevant legal and regulatory developments.

The majority of the audit committee members are members of the South African Institute of Chartered Accountants and are required by the Institute to submit proof of continued professional development on an annual basis. The members interviewed confirmed that they are up to date with this requirement - they cannot risk losing the qualification that they worked so hard for.

4.3 Appointment and Induction

An audit committee is appointed for a period of three years, after which time a new audit committee is appointed. Before the audit committee commences its business, it is inducted in each and every entity. This induction includes, among other things, a workshop on the mandate of the entity; latest risk assessment; a tour of the entity premises and introduction to senior management.

This is considered by many audit committee members as an eye opener in terms of the business of their client. A concern was raised, however, that when there is a vacancy during the three years of service, a member who fills the vacancy does not get a proper induction, and that he/she depends on other members to get an understanding of the entity.

4.4 Knowledge and understanding of AC's roles and responsibilities

A written charter that clearly articulates the committee's purpose, composition, roles and responsibilities, authority and performance assessment plays a key role in directing the committee's activities throughout the year and communicating with stakeholders. Management indicated that the audit committee charter has been reviewed annually by the audit committee.

The external auditors confirmed this and indicated that it forms part of their audit to test if the audit committee charter exists, if it is approved and if it is reviewed annually. Furthermore, external auditors indicated that they are happy that the charters are comprehensive enough. This fulfils the requirement of the Treasury Regulations that each audit committee should have terms of reference which are reviewed annually to ensure relevance.

4.5 Regular attendance of audit committee meetings by members

Regular attendance and full participation of audit committee members at meetings is also a key aspect of their effectiveness. Although members attend audit committee meetings, there is a huge outcry about those who do not regularly attend the meetings. When audit committee members do not attend meetings regularly, they delay the meetings unnecessarily, as some of the resolutions would have been made in meetings where they were absent.

The insights of those members may be crucial during their absence, as members possess different and complementary skills. For example, when a discussion takes place on IT related matters and the member who is an IT expert is not regularly attending meetings, the committee may be limited in terms of executing its responsibilities. In some instances, there is a concern about the lack of courage by audit committee members to raise issues. This could perhaps be an avenue for future research, in order to determine its prevalence among public entities.

4.6 Interaction with assurance providers

Audit committees should meet separately with internal audit and external audit. The audit committee regularly interacts with the assurance providers, namely internal and external auditors, to gain an understanding of the risks encountered by the entities and what measures are put in place to mitigate these risks.

These interactions seek to provide independent communication, without the presence of management. Only one audit committee indicated that they had not met separately with auditors, and that the reasons for this were that the entity is without major issues and there is full cooperation with management. Although this makes sense, from a technical point of view, this audit committee does not comply with the requirement of the PFMA. All other audit committees indicated that they had arrangements to meet with the auditors before or after audit committee meetings.

This practice is over and above the requirement of the PFMA for an audit committee to meet with external auditors separately and on an annual basis. The inconsistent application of this requirement has been noted, however, as some auditors meet with the chairperson only and others meet with the full audit committee. It can be argued that there is nothing wrong with either application, as the chairperson represents the entire audit committee. It is clear that the audit committee also meets regularly with the board to give feedback on its activities.

4.7 Senior Management buy-in

The effectiveness of the audit committee also depends on the attitude of management towards the oversight process of the audit committee. Detailed reports, popularly known as audit committee packs, are submitted to the audit committee to enable members to fully execute their responsibilities. However, there is a problem with the timing of the submission of the audit committee packs, as this has an impact on the preparedness of the audit committee members for the audit committee session. Many entities indicated that reports are not submitted within the agreed upon time frames (e.g. seven days) before the audit committee meeting. There have been instances where incomplete audit packs are submitted and the outstanding documents are submitted during the audit committee meeting.

One audit committee member said the following: “Management needs to embrace the role of audit committees more positively as a governance enhancement tool as opposed to merely trying to comply with PFMA”. Another audit committee member said: “Critical to this is the ‘will’ at the top, the will of management to attend and partake in AC meetings and implement the recommendations of the committee.” Management can be more proactive in their reporting to audit committees, in order to ensure sufficient preparation by the members prior to meetings.

4.8 The responsibility to provide oversight with regard to risk management

The management of the entities hold quarterly sessions where risks are discussed per department. Each department provides its own view and understanding of the risks affecting it. Internal audit is invited to attend the meetings at which management discusses these risks. Internal audit has assisted the audit committees with the identification of emerging risks. It was, however, clear that more emphasis needs to be placed by the committee on rigorously reviewing the risk assessment. One of the audit committee members said as follows: ‘More emphasis on risk management is required.’

The main contributing factor is the combination of the committee’s audit and risk committee into one committee – the audit and risk committee. The interviews revealed that the risk issues are normally put at the end of the agenda and do not receive much attention. One committee member said that in their committee, they have recently changed the agenda to deal with risk issues at the start of the meeting.

4.9 The responsibility to provide oversight with regard to financial reporting

Management needs to be guided in terms of pertinent matters that should be addressed within the organisation. This is mainly done by ensuring a constant focus on an adequate and effective internal control environment. The audit committee has to oversee the accounting and financial reporting processes and the financial statement audits of the companies they serve on.

On a quarterly basis, the audit committees review the quarterly reports that are submitted to the executive authority and Treasury. A special meeting is held between April and May to review the annual financial statements that will be submitted to the Auditor-General for auditing. In this meeting, deliberations are robust to ensure that the audit process does not result in material findings. In this regard, the audit committees were efficient, as most of the selected entities had no material adjustments made to the financial statements submitted for the audit.

4.10 Performance Information

With the advent of the auditing of performance information, public entity audit committees are required to understand the performance drives of a public entity more intimately and ensure that the budgeting process maps these drives and variance analysis. This calls for an approach that is therefore different to that adopted by private sector entities.

As a result of the above, a structured agenda is critical to ensure effective discussion of the key aspects of performance, given the limited time for the scheduled meetings. Therefore, the chairperson of a public entity audit committee is required to be more assertive with management in terms of scheduling the meetings and ensuring that the agenda allows for sufficient time.

4.11 IT Governance

This is one area that has not been fully optimised in public entities due to the complexities in the IT environment, as well as the lack of understanding of IT by the audit committee members themselves. Very few audit committees had a member with a strong background or expertise in the field of IT. In exercising their duty of care, the directors should ensure that prudent and reasonable steps have been taken with regard to IT governance.

In spite of the challenges faced by the audit committee in this regard, the audit committee of most entities did consider IT implications for financial reporting and the going concern assumption. The interviews with internal and external auditors revealed that they have audited IT and submitted findings and recommendations to management. The reports were discussed at the audit committee meeting on the relevant quarterly meeting, and with the use of a tracking document, the audit committee could track the implementation of the recommendations made.

4.12 Compliance with laws and regulations

The audit committee should ensure that the entity complies with all the relevant laws and regulations. Although King III recommends that companies should have a compliance officer, the size of the entities has been identified as very small, with a staff complement of between 30 and

80 for each entity. This poses a challenge for entities when it comes to the suggestion by King III of having a compliance function that is adequately resourced to discharge its responsibilities. The internal audit plays an integral role in auditing compliance with laws and regulations.

The external audit also provides this function to both management and the audit committee. One audit manager from Auditor-General indicated that when the external audit finds non-compliance with financial implications, these are reported in the audit report as irregular expenditure if material - if not material, they are reported only in the management report.

4.13 Sustainability of the public entity

Although King III recommends sustainability reporting, as discussed in chapter 2 of this study, the research found that public sector entities focus mainly on the delivery of pre-determined objectives. The focus on this area is very limited. However, more and more entities are increasingly reporting on economic, social and environmental performance. One of the challenges faced by the entities is the funding of the external assurance provider in terms of the material elements of the sustainability part of the integrated report, as recommended by King III.

4.14 Management of business activities

The interviews with management confirmed that there is a good understanding on their part that policies and procedures are developed and implemented by management. The audit committee and the board play an oversight role in approving the policies developed by management. Some management indicated that the audit committee agenda should focus on governance issues rather than operational issues. Operational issues should be left to the CEO and his/her management team.

The audit committee also guides management on pertinent issues that should be addressed within the entity, and ensures a constant focus on an adequate and effective internal control environment.

4.15 Action plans for addressing weaknesses identified by internal and external audit

In terms of the audit findings, the tracking document has been effective in making both management and audit committee aware of the risks facing the entity. Management reported on a quarterly basis on compliance matters and the resolution of the audit findings raised by both internal and external audit. A concern, however, has been noted, that management simply submits information to the audit committee for compliance purposes and not necessarily to advance and achieve the pre-determined strategic objectives of the entity.

4.16 External auditors: To provide assurance on the adequacy, completeness and correctness of financial reporting

External auditors provide an independent assurance as to whether or not the financial statements comply with the relevant accounting standards and present the financial position and performance of the entity in a fair manner. This complements the internal audit reports, which are provided on a quarterly basis, and the audit committee gains more confidence in fulfilling their reporting requirements, as above. The regulatory audit by the Auditor-General is working effectively and assisting the audit committee in executing its responsibilities.

The Auditor-General plays a pivotal role in the effectiveness of the audit committee, as more and more time is spent with audit committees. With the challenge faced by management and the audit committee as a result of government's requirement that by 2014, all government departments, entities and constitutional institutions and municipalities should have clean audit outcomes, the Auditor-General has assisted the audit committee in identifying critical areas such as IT, and pre-determined objectives that may cause the entities to not achieve the 2014 target.

Audit committees are now able to track these risks and requirements on a quarterly basis. The Auditor-General provides audit committees with dashboard reports to track, on a quarterly basis, the implementation of the recommendations made and solutions proposed by those charged with governance.

The audit committee timeously reviews and provides inputs to the Auditor-General's strategic audit plans. Audit findings raised by the Auditor-General on management and audit reports are tracked and discussed with management on a quarterly basis. 'I have to say because the external auditor's [feedback] is timely; you know what to expect [when], the arrangement is a lot more structured and very clinical'[1].

In line with King III, the chairperson of the audit committee of FPB indicated in the FPB annual report, as well as the audit and risk committee, has reviewed and discussed, with the Auditor General and accounting authority, the audited annual financial statements, the Auditor General's management letter and management responses (Film and Publication Board, 2011).

4.17 Internal audit: To provide the audit committee with assurance pertaining to the adequacy and effectiveness of the processes with regard to corporate governance, risk management and control

The internal audit plays a critical role in the audit committee - it is its eyes and ears. The internal audit provides the audit committee with a risk-based internal audit plan that is directly related to the strategic objectives of the public entity. The internal audit reports are structured in such a way that the report indicates high-risk areas and remedial actions to mitigate those risks. No benchmarking of other public entities as control environments to assist the audit committee to properly consider the severity of the issues raised in the context of other entities was done. Internal audit assists the audit committee in the implementation of risk management tools. Audit committees are provided with the internal audit reports detailing the effectiveness of internal processes in addressing risks and opportunities that enhance business growth and sustainability.

Internal audit provides the audit committee, on a quarterly basis, with reports on the audit work performed for that quarter. Findings raised by internal audit are tracked and the audit committee follows up with management to ensure that they are resolved and that internal audit recommendations are implemented.

Internal audit plays an important role in providing assurance to the audit committee on the effectiveness of controls to mitigate risks. Emerging risks have been identified by the internal audit and were reported to the audit committees. In the 2010/11 annual report, the audit committees were confident about fulfilling their requirement to report on the internal control environment, as the internal audit was reporting on each and every audit committee meeting on the control environment. Internal audit provides the audit committees with objective and unbiased reporting, as they maintain their independence.

The audit committees ensure that the internal audit provides a three-year rolling plan and that annual plans which are risk-based comply with the legislative requirements. Due to the small size of the public entities, the internal audit, for the most part, was outsourced to private audit firms which specialise in internal audit. This ensures that the internal audit is adequately staffed and has relevant skills and expertise to provide audit committees with the guidance they need.

In line with the recommendations of King III, "NERSA's internal audit unit assist management and the audit and risk subcommittee to effectively discharge their responsibilities by means of independent internal control and operational reviews. The internal audit unit reports administratively to the CEO and functionally to the Audit and Risk Subcommittee" (NERSA, 2011: 40).

According to the annual report of FPB, the chairperson of the audit committee indicated that the internal audit coverage plan is risk-based, and this is in line with the recommendations of King III. It is noted in the same report that internal audit reports were reviewed by the audit and risk committee and that this committee has approved the internal audit charter (Film and Publication Board, 2011).

4.18 Independence of assurance providers

In support of the audit committee, the assurance providers (especially internal and external auditors) need to be independent of management. This ensures that internal audits are objective in their reporting. All internal audits reported functionally to the audit committee and administratively to the audit committee. This is in line with best practice and with internal audit charters of the entities selected. Audit committees did not have problems regarding the independence of the assurance providers. However, they raised a concern regarding the in-house internal audit function, which is less likely to be independent, as their salary increases are discussed with and determined by management. This was a concern, especially when there is a power-hungry CEO. In this instance, the audit committee indicated that they directed the external audit to those areas of concern, in order to be more comfortable about the effectiveness of controls. Future research could take this matter forward to find out if there is any merit to the concern of the audit committees.

Interviews with external auditors revealed that the external auditor declares their independence at the beginning and end of the audit to the audit committee. External auditors indicated that this requirement is based on the auditing standards and that each and every individual team member needs to declare his or her independence in writing, and that the engagement manager / senior manager reviews such declarations before the team is assigned to an audit. In a recent 2010/11 audit, a team member had his mother working in the finance department of one of the public entities which he was intending to audit. Due to the perceived independence threat, the team member was assigned to a different public entity. His manager argued that he could have assigned the team member to a different component other than finance, but because of this perceived independence threat, he opted to assign the team member to a completely different audit.

4.19 The accuracy, completeness and fair presentation of financial

In terms of the findings of this study, the financial information submitted to the executive authority through quarterly reports is accurate and complete. The financial statements submitted to the Auditor-General for audit fairly present the financial status of the entity at year end. This also applies to the annual report that the entity issues with the report of the Auditor-General. Although there are changes made to the annual financial statements submitted to the Auditor-General for audit, these have improved in the last two years and changes for the past year were not material. The changes are regarded as a normal audit process. No opinion shopping has been done by the entities in the last two years. This is in line with the recommendation by King III, which discourages opinion shopping.

4.20. Conclusion

Based on the above results, it can be concluded that the audit committees of public entities in Gauteng are effective. The audit committees understand their roles and carry out their responsibilities with the required duty and skill, according to an approved audit committee charter. The audit committee understands its mandate and regularly monitors progress against the set targets and objectives. There is, however, a need to improve on the IT governance implications for the public entities. More emphasis on performance information and risk management is also needed. The frequency of meetings exceeds the requirement of the PFMA, and all agenda items are dealt with.

The length and adequacy of meetings need to be carefully reviewed. There is a clear difference of opinion between management and members of the audit committee in this regard, as management believe that audit committee members want more meetings in order to get more money. Members, on the other hand, argue that the meetings always exceed the recommended time. On average, the recommended time is three hours per meeting and on average, the meetings are exceeded by one and a half hours.

5. RECOMMENDATIONS

Although the PFMA requires the audit committee to have a minimum of two audit committee meetings a year, members feel strongly that management puts a lot of pressure on them to stick to four meetings. However, audit committees could be more efficient in dealing with issues if six meetings could be held during the year.

The PFMA focuses mainly on financial matters, and with the advent of technology, it is important that information technology should be incorporated. The treasury regulations require that the majority of audit committee members are financially literate, but are silent with regard to IT knowledge requirements. This has resulted in little to no attention being paid to information system management issues by audit committees in the public sector. It is therefore recommended that the treasury regulations also incorporate the requirement for audit committee members to include someone with IT expertise.

The PFMA requires the audit committee to meet at least twice a year and currently, the audit committees meet at least four times a year to review quarterly reports. In addition, at least two special audit committees are called during the year. For example, in May, a special audit committee is called to review and recommend the annual financial statements for approval by the board before they are submitted to the Auditor-General or external auditor for auditing. Legislation requires the entities to submit annual financial statements within two months from the end of the financial year to the Auditor-General for auditing. It is therefore recommended that the PFMA be revised to increase the minimum requirement to four times a year.

All public entities fall under government and a benchmarking of other public entities as a control environment could assist the audit committee to properly consider the severity of the internal audit issues raised in the context of other entities.

The audit committee needs to reconsider the flow of the agenda and place risk issues/ reports at the start of the agenda.

Management need to embrace the role of the audit committee more positively as a governance enhancement tool, as opposed to merely trying to comply with the PFMA and treasury regulations. Management can also be more proactive in their reporting to audit committees, in order to ensure that sufficient preparation is done by the members of the audit committee prior to the meetings.

Critical to management is the will at the top. The will of management to attend and partake in audit committee meetings and implement the recommendations of the audit committee is important. Management commitment and proactivity in terms of implementing the right governance structures and ensuring that they are fully resourced with the right people possessing the right skills is very important. In addition, there should be regular management meetings to review and monitor risk, compliance, governance framework and related issues.

The retention strategy should be considered, in order to ensure continuity and sustain the knowledge of the business. A dialogue or communication between assurance providers (external and internal audit), management and the audit committee should be maintained. Management should ensure that quality reports are submitted to the audit committee on time. Furthermore, the agenda of the audit committee meetings should focus on governance issues, rather than operational issues. The latter should be left to the CEO and his/her management team.

Future research could look at the in-house vs outsourced internal audit, in order to determine whether or not there is any merit to the concern of the audit committees that an in-house audit committee could be less independent.

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APPENDICIES

APPENDIX A

List of schedule 3A public entities located in Gauteng

Auditee	Auditee Type
Accounting Standards Board	Schedule 3A/Subsidiary
African Institute of SA	Schedule 3A/Subsidiary
African Renaissance & International Co-operation Fund	Schedule 3A/Subsidiary
Agricultural Research Council	Schedule 3A/Subsidiary
Agriculture Seta (AGRISETA)	Schedule 3A/Subsidiary
Banking Seta (Bankseta)	Schedule 3A/Subsidiary
Boxing SA	Schedule 3A/Subsidiary
Breede River Catchment Management Agency	Schedule 3A/Subsidiary
Chemical Industries Seta (CHIETA)	Schedule 3A/Subsidiary
Clothing,Textiles Seta (CFTL SETA)	Schedule 3A/Subsidiary
Commission for Conciliation, Mediation & Arbitration (CCMA)	Schedule 3A/Subsidiary
Compensation Fund	Schedule 3A/Subsidiary
Competition Commission	Schedule 3A/Subsidiary
Competition Tribunal	Schedule 3A/Subsidiary
Construction Industry Development Board	Schedule 3A/Subsidiary
Construction Seta (CETA)	Schedule 3A/Subsidiary
Co-operative Banks Development Agency	Schedule 3A/Subsidiary
Council for Geoscience	Schedule 3A/Subsidiary
Council for Medical Schemes	Schedule 3A/Subsidiary
Council for the Built Environment	Schedule 3A/Subsidiary
Council on Higher Education	Schedule 3A/Subsidiary
Cross-Border Road Transport Agency	Schedule 3A/Subsidiary
Education Labour Relations Council	Schedule 3A/Subsidiary
Education Seta (ETDP SETA)	Schedule 3A/Subsidiary
Electricity Distribution Industry Holdings (Pty) Ltd	Schedule 3A/Subsidiary
Energy Seta (ESETA)	Schedule 3A/Subsidiary
Estate Agency Affairs Board	Schedule 3A/Subsidiary
Film & Publication Board	Schedule 3A/Subsidiary
Financial Services Board	Schedule 3A/Subsidiary
Financial Seta (FASSET)	Schedule 3A/Subsidiary
Food & Beverages Seta (FOODBEV)	Schedule 3A/Subsidiary
Forest Industries Seta (FIETA)	Schedule 3A/Subsidiary
Freedom Park	Schedule 3A/Subsidiary
Health & Welfare Seta (HWSETA)	Schedule 3A/Subsidiary
Housing Development Agency	Schedule 3A/Subsidiary
Human Science Research Council	Schedule 3A/Subsidiary
Independent Regulatory Board for Auditors	Schedule 3A/Subsidiary
Information Systems Seta (ISETT)	Schedule 3A/Subsidiary
Inkomati Catchment Management Agency	Schedule 3A/Subsidiary
Insurance Seta (INSETA)	Schedule 3A/Subsidiary
International Marketing Council	Schedule 3A/Subsidiary
International Trade Administration Commission (ITAC)	Schedule 3A/Subsidiary
Legal Aid South Africa	Schedule 3A/Subsidiary
Local Government Seta (LGWSETA)	Schedule 3A/Subsidiary
Manufacturing & Engineering Seta (MERSETA)	Schedule 3A/Subsidiary
Market Theatre Foundation	Schedule 3A/Subsidiary

Auditee	Auditee Type
Media & Publishing Seta (MAPPP SETA)	Schedule 3A/Subsidiary
Media Development and Diversity Agency	Schedule 3A/Subsidiary
Mine Health and Safety Council	Schedule 3A/Subsidiary
Mining Qualifications Authority (MQA)	Schedule 3A/Subsidiary
National Agricultural Marketing Council	Schedule 3A/Subsidiary
National Arts Council of South Africa	Schedule 3A/Subsidiary
National Consumer Tribunal	Schedule 3A/Subsidiary
National Credit Regulator	Schedule 3A/Subsidiary
National Development Agency	Schedule 3A/Subsidiary
National Economic Development and Labour Council (Nedlac)	Schedule 3A/Subsidiary
National Electronic Media Institiute of SA	Schedule 3A/Subsidiary
National Empowerment Fund	Schedule 3A/Subsidiary
National Energy Regulator of South Africa (NERSA)	Schedule 3A/Subsidiary
National Film and Video Foundation of South Africa	Schedule 3A/Subsidiary
National Gambling Board	Schedule 3A/Subsidiary
National Heritage Council	Schedule 3A/Subsidiary
National Home Builders Registration Council	Schedule 3A/Subsidiary
National Housing Finance Corporation Ltd	Schedule 3A/Subsidiary
National Library of South Africa	Schedule 3A/Subsidiary
National Lotteries Board	Schedule 3A/Subsidiary
National Metrology Institute of SA	Schedule 3A/Subsidiary
National Nuclear Regulator (NNR)	Schedule 3A/Subsidiary
National Regulator for Compulsory Specifications	Schedule 3A/Subsidiary
National Research Foundation	Schedule 3A/Subsidiary
National Urban Reconstruction & Housing Agency	Schedule 3A/Subsidiary
National Youth Development Agency	Schedule 3A/Subsidiary
Ombudsman for Financial Services Providers	Schedule 3A/Subsidiary
Pension Funds Adjudicator	Schedule 3A/Subsidiary
Perishable Products Export Control Board	Schedule 3A/Subsidiary
Private Security Industry Regulatory Authority	Schedule 3A/Subsidiary
Productivity SA	Schedule 3A/Subsidiary
Public Sector Seta (PSETA)	Schedule 3A/Subsidiary
Railway Safety Regulator	Schedule 3A/Subsidiary
Road Accident Fund	Schedule 3A/Subsidiary
Road Traffic Management Corporation	Schedule 3A/Subsidiary
Robben Island Museum	Schedule 3A/Subsidiary
Rural Housing Loan Fund	Schedule 3A/Subsidiary
SA Civil Aviation Authority	Schedule 3A/Subsidiary
SA Maritime Safety Authority	Schedule 3A/Subsidiary
SA National Accreditation System	Schedule 3A/Subsidiary
Safety & Security Seta	Schedule 3A/Subsidiary
SARS - Administered Revenue	Schedule 3A/Subsidiary
SARS - Own Accounts	Schedule 3A/Subsidiary
Servcon Housing Solutions (Pty) Ltd	Schedule 3A/Subsidiary
Service Sector Education and Training Authority	Schedule 3A/Subsidiary
Small Enterprise Development Agency (SEDA)	Schedule 3A/Subsidiary
Social Housing Foundation	Schedule 3A/Subsidiary
South Africa Diamond and Precious Metals Regulator	Schedule 3A/Subsidiary
South African Council of Educators	Schedule 3A/Subsidiary
South African Local Government Association	Schedule 3A/Subsidiary
South African National Parks	Schedule 3A/Subsidiary

Auditee	Auditee Type
South African National Roads Agency Limited	Schedule 3A/Subsidiary
South African National Space Agency (SANSA)	Schedule 3A/Subsidiary
South African Qualifications Authority	Schedule 3A/Subsidiary
South African Social Security Agency	Schedule 3A/Subsidiary
South African Tourism	Schedule 3A/Subsidiary
South African Weather Service	Schedule 3A/Subsidiary
Special Investigating Unit	Schedule 3A/Subsidiary
State Information Technology Agency	Schedule 3A/Subsidiary
State Theatre	Schedule 3A/Subsidiary
Technology Innovation Agency (TIA)	Schedule 3A/Subsidiary
Thubelisha Homes	Schedule 3A/Subsidiary
Tourism & Hospitality Seta (THETA)	Schedule 3A/Subsidiary
Transport Seta (TETA)	Schedule 3A/Subsidiary
Umalusi QA on Further Training & Education	Schedule 3A/Subsidiary
Unemployment Insurance Fund	Schedule 3A/Subsidiary
Universal Service Agency (USAASA)	Schedule 3A/Subsidiary
Universal Service Fund (USAAF)	Schedule 3A/Subsidiary
Water Research Commission	Schedule 3A/Subsidiary
Wholesale & Retail Seta (W&R SETA)	Schedule 3A/Subsidiary
Windybrow Theatre	Schedule 3A/Subsidiary

APPENDIX B

Dr. T Ramontja
The Chief Executive Officer
Council for Geoscience
280 Pretoria Street
Silverton
Pretoria

22 August 2011

Dear Sir

MASTERS BUSINESS LEADERSHIP: THESIS

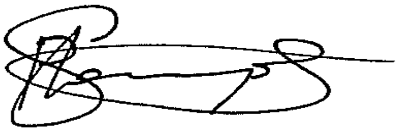
I am a final year Masters in Business Leadership (MBL) student at UNISA Graduate School of Business Leadership. As part of my studies I am required to make a research on the topic of my choice. My research topic is "An analysis of audit committees' effectiveness at public entities in Gauteng". CGS is one of the entities that I have chosen for this research. I therefore, request your permission to conduct the research at your entity.

The research will include you, audit committee members and mainly invitees to the audit committee meetings. I will observe any confidentiality requirements as requested regarding any information made available to me in assisting with this study.

On completion of this study, a copy of the report will be presented to you. I will then return the copies used for examination purposes to you, **if required.**

I thank you for your willingness to be of assistance.

Yours Faithfully



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