



AUDITOR - GENERAL
SOUTH AFRICA



Auditing to build public confidence

**DEPARTMENT OF SMALL BUSINESS DEVELOPMENT
INVESTIGATION FEEDBACK
4 NOVEMBER 2020**

REPUTATION PROMISE/MISSION



The Auditor-General of South Africa (AGSA) has a constitutional mandate and, as the Supreme Audit Institution (SAI) of South Africa, exists to strengthen our country's democracy by **enabling oversight, accountability and governance** in the public sector through auditing, thereby **building public confidence**.



BACKGROUND

- The Auditor-General approved the investigation at the Department of Small Business Development in 2018. A letter of engagement in respect of the investigation was signed on 23 March 2018 with the former DG of the department.
- The investigation focussed on the **2015-16** and **2016-17** financial years.
- The scope of the investigation included:
 - Compliance of the DSBD to the guidelines and standard operating procedures (SOP) of the Black Business Supplier Development Programme (BBSDP) and Co-operative Incentive Scheme (CIS);
 - The validity of the processes followed in awarding incentives to grant applicants;
 - Confirmation of the authenticity of suppliers and quotations;
 - Verification that goods and services were actually delivered/received; and
 - Monitoring and reporting processes followed by the DSBD subsequent to the approval and payment of the incentives to the beneficiaries.



INTRODUCTION



BBSDP

- During the 2015-16 year, 684 applications for BBSDP grant funding were approved (approximately R307 million). 597 of these were paid in the year (approximately R193 million).
- During the 2016-17 year, 738 applications for BBSDP grant funding were approved (approximately R392 million). 598 of these were paid in the year (approximately R242 million).
- The findings are predominately due to non-adherence to the BBSDP guidelines and SOP in processing, evaluating, adjudicating and recommending grant applicants for approval of the incentive schemes. The findings also point to inadequate internal controls, monitoring and oversight in the awarding of incentives to grant applicants.



INTRODUCTION cont...



CIS

- The total value of approved applications for CIS grant funding for the 2015-16 financial year amounted to approximately R84,4 million, of which R74,9 million was paid.
- The total value of approved applications for CIS grant funding for the 2016-17 financial year amounted to approximately R65,7 million, of which R63,8 million was paid.
- The findings in respect of the CIS are predominately attributable to the non-adherence to the CIS guidelines and SOP in processing, evaluating, adjudicating and recommending grant applicants for approval of the incentive schemes. The findings also point to inadequate internal controls, monitoring and oversight by the DSBD in the awarding of incentives to grant applicants.



FINDINGS cont...



Non-compliance to incentive schemes guidelines and SOPs

BBSDP:

- The AGSA inspected 88 application files. 37 (42%) of these contained no evidence that inspections had been performed before submission of the applications to the adjudication committee for approval, in contravention of the BBSDP guidelines. All 37 applications were approved by the adjudication committee. Eight officials were implicated in this regard.



FINDINGS cont...



Non-compliance to incentive schemes guidelines and SOPs

- 23 out of 88 applications (26%) of the sample tested were accepted and approved despite the application amounts exceeding 30% of the applicant's previous year turnover (according to the financial statements) or there was no evidence to substantiate the 30% previous year turnover requirement, in contravention of the BBSDP guidelines/ SOP. Four officials were implicated in this regard.
- 34 of the 88 (39%) application samples investigated did not contain the required documentation relating to the requirement for copies of Identity documents (IDs) of key managers, directors, shareholders and list of employees of the entity, in contravention of the guidelines. Officials submitted these applications to the adjudication committee and they were approved without the required documentation. Six officials were implicated in this regard.



FINDINGS cont...



Non-compliance to incentive schemes guidelines and SOPs

- According to the financial statements from the sample selected, 16 out of the 88 (18%) applications did not have the financial capacity to fund 50% of the total cost of equipment applied for as their current liabilities greatly exceeded current assets. Furthermore, the diagnostic reports prepared by NFs in most instances did not indicate how the applicant's 50% contribution will be funded.
- 19 out of 72 claims (26%) tested were paid without the requisite documentation. Five officials were implicated in this regard.



FINDINGS cont...



Non-compliance to incentive schemes guidelines and SOPs

CIS:

- For 9 of the 58 (16%) applications investigated the Trade and Industry Advisor (TIA) did not perform site visits prior to submitting applications to adjudication committee. One official was implicated in this regard.
- 20 of the 58 (34%) applications investigated were processed and approved without the required documentation. Five officials were implicated in this regard.
- For 4 of the 58 (7%) applications investigated the TIAs did not confirmed that three quotations were submitted for each activity applied for. Three officials were implicated in this regard.
- For 2 of the 58 (3%) applications investigated the lowest quotation was not accepted, without documenting reasons for not accepting the lowest quotation. Two officials were implicated in this regard.
- 12 of the 58 (21%) applications were approved by the adjudication committee with less than three quotations however the motivation for deviations were not approved by the AO. One official was implicated in this regard.



FINDINGS cont...



Validity of awarding BBSDP incentives

- 34 grant applicants that had a turnover above R1 million, however these applicants were not registered for VAT .
- We noted multiple instances where preferred service providers that quoted above R1 000 000 did not include VAT in their quotations. They also failed to provide their VAT registration number on their quotations. These quotations, amounting to R12 050 625 were accepted by the BDOs.
- One supplier was registered for VAT according to the SARS website but did not charge VAT on their invoice. The invoice was for an amount of R1 360 000.
- During the investigation we identified that directors of multiple companies applied for and received grants exceeding the R1 million threshold .



FINDINGS cont...



Verification that goods and services were delivered/received by the BBSDP grant applicant

- The AGSA performed site visits at the premises of 50 approved grant applicants. In 32 of the 50 (64%) site visits, the AGSA was unable to locate or verify the existence of such premises and/or assets for which the grant funding was provided. DSBD paid R19 921 877 to these 32 entities.
- Three different grant applicants indicated the same address on application forms and the inspection report compiled by the BDO for one of these applicants confirmed the address. The AGSA investigation team visited the address and confirmed the address belongs to a homeless shelter. A total amount of R1 287 720 was paid to two of these grant applicants at the draft management report (22 February 2019).



FINDINGS cont...



Verification that goods and services were delivered/received by the BBSDP grant applicant (cont...)

- One instance was noted where a grant applicant applied for and was paid an incentive for equipment amounting to R800 000. The inspection report contained photos of a digital packing machine reflecting the serial number of the equipment. During the AGSA inspection an old analogue machine was found on site, with a serial number which corresponded to the pictures on file. However, the equipment differed.
- In three instances, grant applicants received incentives for weighbridges amounting to R2 400 000. The inspection reports indicated that equipment had been delivered to the applicants. The AGSA visited the premises and determined that the weighbridges belonged to other third parties and not the applicants .



FINDINGS cont...



Verification that goods and services were delivered/received by the CIS grant applicant (cont...)

- The AGSA selected 10 co-operatives of the 58 sampled to physically verify whether the entities existed and if goods and services were actually delivered. Of the 10 co-operatives, the AGSA was unable to verify the existence of five of them (50%). The amount paid by DSBD to the five co-operatives amounted to R 1 692 792.



FINDINGS cont...



Monitoring and reporting processes followed by DSBD subsequent to the approval of the grant applicants

- It was confirmed by the BBSDP Director and BBSDP Deputy Director that no post-approval site visits were conducted for the BBSDP applications approved and paid.
- It was also confirmed by the CIS Deputy Director that the DSBD does not conduct post investment site visits on funded co-operatives.



FINDINGS cont...



Possible fraudulent BBSDP claims cont...

- Another grant applicant procured imported machinery from a service provider based in the USA. However, we noted that the machinery differed from the photo evidence submitted with the inspection report and that the machinery was manufactured in 2010 by a Chinese based company. This suggests that the applicant possibly already owned the machinery before applying for the grant. Furthermore, there is a possible conflict of interest between the grant applicant and the service provider in that the director/member of the grant applicant and the director of the service provider appear to be spouses based on their social media profiles.



FINDINGS cont...



Possible fraudulent BBSDP claims cont...

- Four separate grant applicants applied for grants from DSBD during 2014 to 2016. DSBD paid grants totalling R3 118 411 to these four entities. Results from the inspection of the claim files and CIPC searches is suggestive of the possibility that the four entities are connected. The BDOs that performed the site visits relating to these claims indicated in the inspection reports that the equipment was delivered however, when the AGSA visited the address indicated on the BBSDP inspection report, there was no sign of such businesses at the indicated address.



REPORTING



- A draft management report was compiled and issued to the Accounting Officer (AO) on 22 February 2019 and discussed with the AO and Executive Authority on 28 February 2019.
- On 28 February 2019, the AGSA discussed the investigation and findings with Minister Zulu.
- DSBD management provided responses on our findings and recommendations on 19 and 25 March 2019.
- A final management report (incorporating management responses) was issued to the AO on 25 April 2019.



MANAGEMENT RESPONSE TO DRAFT MANAGEMENT REPORT

- Management has indicated that they will arrange training for all officials working with the processing of applications and claims to ensure compliance. Training interventions will comprise of the following:
 - Continuous refresher training to ensure that staff are updated on all new developments.
 - A suitable course to retrain all the TIAs has been sourced and SCM processes are in process to appoint a training provider.
 - The DSBD HR Unit is assisting with the process and it is envisaged that training will resume in the first quarter of the new financial year 2019/20.
- Management intends to institute disciplinary action against officials for non-compliance with the BBSDP guidelines.



MANAGEMENT RESPONSE TO DRAFT MANAGEMENT REPORT

cont...

- Management also intends to open cases of fraud against the officials, grant applicants and service providers with the South African Police Service.
- Management has decided to blacklist NFs that appear to have made misrepresentations in diagnostic reports and potentially colluded with officials.
- Furthermore, management will consider deregistering NFs that did not qualify to be registered as NFs or did not submit all required documentation.



WAY FORWARD

- On 25 April 2019, the acting DG requested assistance from the AGSA in providing information and evidence that was solicited during the investigation. As well as for the investigators to provide testimonies at the disciplinary hearings.
- On 29 April 2019, the AG acceded to the request.
- AGSA subsequently provided the DSBD with relevant information/ evidence as well as input on the disciplinary charges, this process continued until December 2019.
- Disciplinary processes were scheduled to take place beginning 2020 but was halted due to Covid19.
- Disciplinary processes subsequently proceeded and in October 2020, the investigators were called to provide testimonies. This process is ongoing and further hearing dates have been scheduled for November 2020.
- A public report will be issued, on completion of the disciplinary processes.



DEPARTMENT OF SMALL BUSINESS DEVELOPMENT INVESTIGATION FEEDBACK

