PART 5:

Annual Financial Statements

For The Year Ended 31 March 2003

CONTENTS

MANAGEMENT REPORT

FOR THE YEAR ENDED 31 MARCH 2003

Report by the accounting officer to the executive authority and Parliament of the Republic of South Africa.

1 GENERAL REVIEW OF THE STATE OF FINANCIAL AFFAIRS

1.1 INTRODUCTION

The Department of Foreign Affairs (department) is responsible for the formulation, application and execution of all aspects of South Africa's foreign policy as entrusted to the Minister of Foreign Affairs (minister). Liaison with foreign governments on matters of international relations is effected through South Africa's accredited representatives. The head of a South African mission abroad acts as the representative of the head of state. During the year under review, the department increased its foreign representation by opening six additional missions in Africa, Asia and the Middle East regions as reflected hereunder:

SOUTH AFRICAN MISSIONS

Region	1990/00	2000/01	2001/02	2002/03
Africa	25	25	28	30
Asia & Middle East	21	21	21	25
America	16	16	16	16
Europe	25	23	23	23
Multilateral	3	4	4	4
Total	90	89	92	98

Total number of missions 2002/2003 = 98

In line with the Public Finance Management Act, 1999 (Act No. 1 of 1999 as amended) (PFMA) and the Treasury Regulations, the department submitted its strategic plan for the medium term expenditure framework (MTEF) period 2002/03 to 2004/05 and identified the following strategic priorities for implementation during the year under review:

- Facilitating the successful transition of the Organisation of African Unity (OAU) to the African Union (AU);
- Working towards the restructuring of the Southern African Development Community (SADC) and the physical creation of the SACU institutions;

- Focusing on the implementation of the new partnership for African development (NEPAD);
- Working towards peace, stability and security;
- Facilitating sustainable foreign direct investment, international trade, tourism and environmental conservation; and
- Focusing on imaging and branding.
- In order to align the resources of the department to its strategic priorities and to enable the department to comply with the new monitoring, evaluation and reporting processes introduced by government, the programmes were revised as follows:
- *Administration* provides for the overall policy development, execution and management of the department.
- *Foreign Relations* involve the promotion of relations with countries, and participation in international organisations and institutions, in pursuit of South Africa's national values and foreign policy objectives.
- *Public Diplomacy and Protocol* promote an understanding, both domestically and internationally, of South Africa's foreign policy objectives, project a positive image of South Africa's role and position in international relations and provide protocol services.
- *Foreign Properties* provide secure, economical housing and office accommodation to all staff members abroad and maintain immovable property abroad.
- *Auxiliary and Associated Services* provide for the payment of membership fees to international organisations, transfer payments and support services for all officials on transfer abroad, and make provision for the inauguration of the president of South Africa.

This report seeks to assist in measuring the extent to which the department's resources allocated for the 2002/03 financial year were utilised in terms of the PFMA.

1.2 REVENUE

During the year under review, the department received total revenue of **R2,521** billion made up of voted funds and non-voted funds, as set out hereunder: -

Voted funds – R2,451 billion

- **Charge to the National Revenue Fund (R2,407 billion)**

The department received a budget allocation of R2,407 billion for the 2002/03 financial year, which showed a 13,32% increase against the budget allocated for the 2001/02 financial year. The budget increase can be attributed to additional funding (R250 million) received for specific items; R170 million, which was a South African contribution to SADC countries for food shortages through the World Food Programme (WFP) administered by the United Nations (UN) and R80 million for the implementation of the new Foreign Service Dispensation. During the adjustment estimates an additional amount of R67 million was received. The amount received was utilised for the inaugural summit of the AU (R37 million), South Africa's term as chairperson of the AU (R6 million), the establishment of the Democratic Republic of the Congo (DRC) secretariat (R10 million), the NEPAD secretariat (R5 million) and the Commonwealth Fund for Technical Co-operation (R9 million).

As reported in the previous financial year, the department requested for a roll-over of funds (R129 million) in respect of specific commitments, which was approved. The roll-over was in respect of the Non-Aligned Movement Summit (R26 million), taxation of foreign allowances (R10 million) and capital works (R93 million). In addition, an amount of R14 million was allocated for the contribution to the NEPAD secretariat.

It should be noted that some of these amounts do not form part of the baseline amount. Hence it can be regarded as once-off. Taking this into account, the budget for 2002/03 has actually decreased in real terms as compared to the budget of the 2001/02 financial year.

- **Appropriation for unauthorised expenditure (R44 million)**

For the past financial years, the department has been reporting unauthorised expenditure (R57,412 million) in respect of previous years: R8,380 million (excess expenditure 1998/99), R35,896 million (excess expenditure 1999/2000), R6,358 million (excess expenditure 2000/01) and R6,778 million (TBVC salary claims). During the year under review, Parliament has authorised the expenditure and approved additional funding (R44 million) in respect of the excess expenditure. However, in respect of the TBVC salary claims, Parliament approved that voted funds of the department be utilised to off-set the expenditure.

Non-voted funds – R70 million

- **Other revenue to be surrendered (R67 million)**

Other revenue relates to revenue received in respect of ad hoc activities, as the department does not have any income-generating programmes. During the year under review, the department sold a building in Paris for R29 million, which was previously used by the then Bophuthatswana government. The other R27 million is in respect of value-added tax (VAT) claims as missions in other countries are allowed to reclaim VAT. The remaining balance is proceeds from sale of equipment, interest received, stale cheques written back, etc., detailed in note 2 to the income statement.

- **Local and foreign-aid assistance (R3 million)**

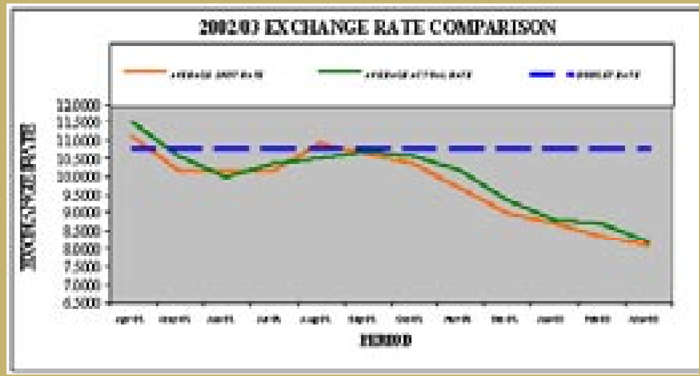
As previously reported, our mission in London hosted a project "Celebrate South Africa" aimed at promoting South Africa in the United Kingdom (UK). The project was funded through donors and a total amount of R21 million was received during the 2001/02 financial year. However, there were still outstanding pledges to be collected for the Celebrate South Africa project and the World Conference Against Racism (WCAR).

1.3 EXPENDITURE

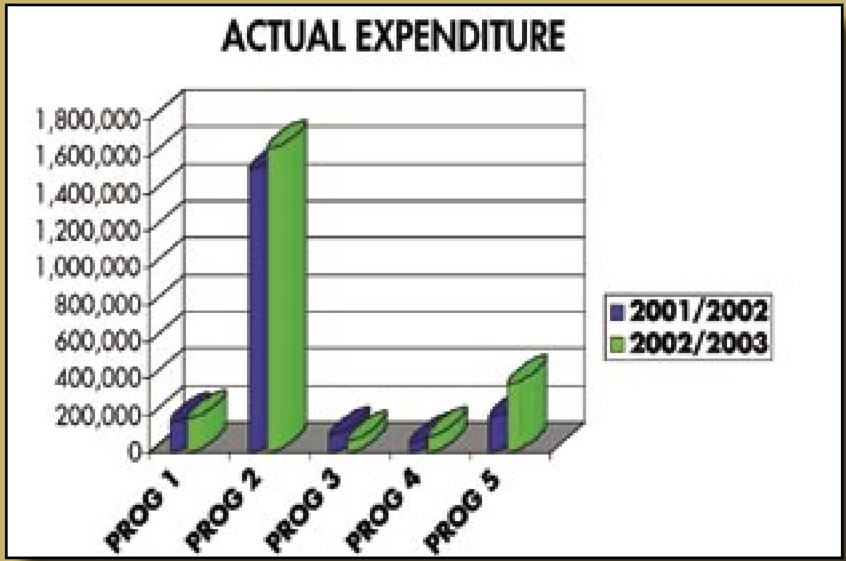
Spending trends

South Africa maintains diplomatic relations with countries and organisations through 98 missions in 85 countries located throughout the world. Therefore the bulk of its expenditure is incurred in foreign currencies. This poses a major risk with regard to budgetary controls as the department has no control over the fluctuation of the Rand against major foreign currencies. Due to this unpredictable or uncontrolled situation, the department can either overspend or underspend its budget. However, the department has reached an understanding with the National Treasury to use the fixed exchange rates determined by the treasury for budget purposes. Therefore, if there is a difference between the actual performance of the Rand and the budgeted rate, the allocated budget is adjusted accordingly. In the event of a depreciation of the Rand (lower than the fixed rate determined by the National Treasury) the adjustment estimate process is the only avenue available for the department to be provided with resources to compensate for exchange rate losses. Should depreciation of the Rand take place after the adjustment estimate process, the department has to fund such losses from within its allocated resources.

During the year under review, the Rand has performed fairly well as against major foreign currencies. As shown in the graph below the budget exchange rate has been higher than the average spot rate, and the spot rate at which we bought dollars has also been lower: -



Over the years the expenditure on the vote as a whole has been increasing by an annual average of 5%. However, there was a considerable jump during the 2001/02 financial year of approximately 27% compared to previous financial years. During the year under review, the expenditure has increased by 14.73 %. This increase can be attributed to the unique role that has been imposed on South Africa as a torchbearer for the revitalisation of the African continent. This includes our involvement in peace processes, development of NEPAD, South Africa's role as the chairperson of the AU, etc. As shown in the graph below, the major increase is in programme 2 as a result of our international responsibilities and commitments, and programme 5 due to the R170 million paid to the UN for the WFP, as well as South Africa's contribution to the NEPAD secretariat:



During the year under review, the department utilised 94,34% of the total budget allocated for the 2002/03 financial year. Savings realised can be attributed to unspent funds in programme 2: Foreign Relations and programme 4: Foreign Properties. It is important to report that the department had in fact not realised any savings since this amount is already committed as follows: -

- Foreign Service Dispensation (FSD) – R90 million

  The Department of Public Service Administration was mandated by cabinet to investigate and implement a Foreign Service Dispensation (allowances for employees serving abroad) that would be fair, affordable and equitable. During the year under review, negotiations were finalised with the unions and agreement signed in this regard. However, due to fundamental difficulties, the new Foreign Service Dispensation was not implemented. The Department of Public Service Administration, the National Treasury and the department are looking at this matter with a view of finding a lasting solution.

- Equipment – R8 million

  The department was involved in a process of opening missions in Muscat and Doha. However, there were delays beyond the department's control in the refurbishment of the chanceries. Computers and other equipment have already been ordered.

- Capital projects – R43 million

  These savings are attributed to projects taken over from the Department of Public Works in Kinshasa and Berlin. These projects will be finalised during June 2003 and March 2004, respectively.

The department has already submitted a request for the roll-over of funds to the National Treasury in respect of these savings. Taking the above into account, the department has managed its financial affairs reasonably well. However, there was an over-expenditure of R6, 880 million as reflected in programme 3. This expenditure must be classified as unauthorised expenditure in terms of the PFMA, chapter 1, "unauthorised expenditure". It is also important to report that this amount was supposed to be allocated against unauthorised expenditure. However, due to the closure of the financial management system (FMS) this transaction will be processed in the next financial year. The same process was followed in respect of 2001/02 over-expenditure.

2. UTILISATION OF DONOR FUNDS

As reported last year, the department hosted a Celebrate South Africa event, which was organised by our mission in London during May 2001, to promote South Africa in the UK. The project was financed through secured sponsorships, although it was an objective of the department (imaging and branding). In terms of the project there were certain activities such as digital video display sales and television rights which were intended to raise some funds over a period of four years.

During the year under review, an amount of R2,9 million has been received, but not yet claimed from the RDP account. Therefore, there is an outstanding balance of R683 000 not yet cleared as against the balance of R3,5 million during the last financial year. In addition, an amount of R4,4 million has been received in respect of the WCAR and the United Nations Development Program (UNDP), but not yet claimed from the RDP account.

3. OTHER ORGANISATIONS TO WHOM TRANSFER PAYMENTS HAVE BEEN MADE

Transfer payments primarily arise from obligations undertaken by South Africa at international, regional and sub-regional multilateral levels. The payments, which are made by the department, generally take the form of: -

- Membership dues to organisations such as the UN, the OAU, the SADC, the Commonwealth, etc.
- Contributions to peacekeeping operations of the UN.
- Meetings of state (parties to international treaties) of which South Africa is a member, and in which South Africa has participated.
- Voluntary pledges that South Africa has made to international organisations for the purpose of humanitarian assistance, technical assistance, etc.

In the context of the UN, South Africa's assessed contributions to the regular budget are calculated at 0,41% of the total budget, while peacekeeping contributions are calculated at a 'developing country discounted rate' of 20% of 0,41% of the total cost of each specific UN peacekeeping operation. Contributions to other UN organisations, treaty bodies, etc. are determined on the basis of the calculation for South Africa's contribution to the UN regular budget as adjusted to the membership of the particular organisation or body.

The Development Bank of Southern Africa (DBSA) was requested by the presidency to establish the NEPAD secretariat. The NEPAD initiative is a pledge by African leaders to eradicate poverty and to place their countries, both individually and collectively, on a path of sustainable growth and development and, at the same time, to participate actively in the world economy and body politic.

The DBSA agreed to this request and initially entered into a memorandum of understanding (MOU) with the presidency to act, as agent, on behalf of the NEPAD secretariat in terms of all NEPAD's contractual, financial, administrative and certain logistical needs and requirements. Therefore the receipt and disbursement of funds are administered by the DBSA on behalf of NEPAD.

During the adjustment estimates, the department was allocated resources to partially fund the NEPAD secretariat. To date, NEPAD's activities have been funded by international donor funding, private sector sponsorships and through a bridging facility supplied by the DBSA. The South African government contributed R2 million during the 2001/02 financial year and R14.1 million has been transferred to the NEPAD secretariat during the year under review. A memorandum of understanding between the department and the DBSA is being finalised.

During June 2002, the WFP conducted an assessment on behalf of the UN and quantified the amount of emergency food assistance that was needed to avert widespread deaths through starvation. The monetary value of the need was US$611 million.

On 18 July 2002, the WFP issued an international appeal on behalf of the UN for assistance to deal with food shortages across the world. At the SADC Summit in Luanda in October 2002 president Mbeki announced that South Africa would contribute 100 000 tons of maize to be delivered to the WFP for distribution to SADC countries. An amount of R170 million was transferred to the UN as South Africa's contribution to meet its commitment to provide the 100 000 tons of maize to the WFP.

The WFP has already disbursed most of the funds in effecting purchases from local grain mills and has exported most of the 100 000 tons of grain. The balance is in the process of being purchased on local markets and will be delivered to recipients in the next financial year.

With regard to accountability, these organisations and institutions prepare detailed financial statements which are subject to auditing and public scrutiny.

4. SERVICES RENDERED BY THE DEPARTMENT

Consular services

Consular services reflect the mandate of the South African government to provide assistance and protection to its citizen's abroad. Consular matters can be summarised as services provided by the department in terms of the 1963 Vienna Convention on Consular Relations.

During the year under review, the department was also involved in a number of cases pertaining to South African citizens detained abroad (statistics at present: approximately 713 detainees/prisoners). Consular services rendered to the public include visitation of injured, hospitalised and detained/imprisoned South African citizens abroad. These consular services involve mission personnel abroad having to travel to destinations where these services have to be rendered. Often the rendering of consular services is unplanned and this means that the department incurs expenses that it was unable to accurately provide for.

In addition, the department assisted South African citizens after the 12 October 2002 Bali bomb blasts by locating 90 reportedly missing citizens and informing family members accordingly.

Agency services

Agency services are services rendered on behalf of other government departments, which are either not represented abroad or only represented at some missions. These departments include Home Affairs, Justice, Welfare, Transport, Agriculture, the South African Revenue Services and Trade and Industry. The directorate primarily supports the Department of Home Affairs with services that include passport processing, visas, work and study permits. Where the services being rendered require a fee, collection and payment are managed according to the relevant department's requirements and in accordance with treasury guidelines and regulations.

In addition, the department is the custodian of the QED payroll system, which is used to process allowances payable to transferred officials, including those of other departments. This service to other departments takes place on an agency basis. The department therefore incurs the expenditure on a recoverable basis.

Legalisation functions

A large percentage of the work at head office involves the legalisation/authentication of official documents for use abroad. The documents are either affixed to an Apostle (where countries are party to the Hague Convention of 1961) or to a Certificate of Authentication. Between 1 000 and 1 200 documents are handled/processed by the legalisation section per month.

African Renaissance and International Co-operation Fund

The department, in consultation with the National Treasury, is also responsible for the administration of the African Renaissance and International Co-operation Fund (fund).

The fund is under the control of the Director-General: Foreign Affairs who, as the accounting officer, keeps records and accounts of all payments into and out of the fund. An Advisory Committee was appointed to make recommendations to the Ministers of Foreign Affairs and Finance on the disbursement of funds, as provided for in the African Renaissance and International Co-operation Fund Act, 2000 (Act No. 51 of 2000) (act). Due to the urgency of some of the projects as well as the lengthy process to be followed to finalise the projects, the department had to utilise its funds on the approval of the Acting Director-General or the Minister. This is done with a view of claiming it back from the fund once a letter of concurrence has been received from the Minister of Finance. This has resulted in the opening of a receivables account in the books of the department and a payables account in the trust fund's books of account.

During the year under review, the department has utilised approximately R39,465 million of its funds, of which letters of concurrence from the Minister of Finance are still awaited. This arrangement poses a risk to the department, as the amount owed by the fund is not enforceable in the event that the Minister of Finance does not issue the letters of concurrence.

Due to the nature of the projects funded and the administrative processes to be followed, it is the view of the department to propose some amendments to the act.

The financial statements of the fund are attached as Annexure A.

5. CAPACITY CONSTRAINTS

As reported already, the department is responsible for co-ordinating and leading the entire spectrum of South Africa's interaction with the world. Its activities are therefore multifunctional, varied and complex. During the last financial year, the department conducted an in-depth analysis of its activities both at head office and at missions to determine its capacity requirements in terms of the challenges it faces (the capacity building project). This analysis focused on the department's needs in terms of systems, processes, infrastructure and human resources. The conclusion was that the department lacks capacity to fulfil its role as custodian of South Africa's international relations and obligations. Due to scarce resources, the department resolved to implement the project in different phases.

Good progress has been made with some elements of the project, taking into account the limited available funding. With regard to the filling of posts, the implementation of Resolution No.7, which deals with the transformation and restructuring of the Public Service, placed a moratorium until certain processes were complete. Therefore, the department was unable to fill all its vacant funded posts during the year under review. However, the department has made good progress in this regard and it will be able to fill these positions in the next financial year.

6. CORPORATE GOVERNANCE ARRANGEMENTS

The department continues with its endeavours to subscribe to the principles of openness and integrity, more especially in the area of corporate governance. In this regard the department ensures that its processes and practices are transparent, that utilisation of resources is economical, efficient and effective, and benchmarked with international best practices.

Risk management approach

The department complies with a risk-based approach to internal control systems. During the year under review, a number of business processes were documented and analysed, and the result of the risk analysis updated. The complexity of the department and the fact that it has to comply with certain security requirements resulted in this exercise being restricted to the corporate service branch only. In the new financial year a full risk assessment will be conducted throughout the department with the assistance of internal audit.

A risk profile for the department and the internal audit operational plan (taking into consideration the risk profile) has been developed.

Fraud prevention policies

During the year under review, the department developed a departmental fraud prevention strategy and a fraud prevention plan. Management and the audit committee extensively reviewed these policy documents, and the audit committee accepted the strategy and the policy.

The department is currently busy developing a fraud operational plan in order to implement the strategy and the policy. A tender for an anti-corruption and fraud hotline has been prepared and this will be advertised in the new financial year.

Audit committee and internal audit

The audit committee remained at three members and was functional throughout the year under review. The chairperson of the audit committee and the majority of the members are from outside of the public sector. The audit committee approved the internal audit business plan, strategic plan and operational plan as well as the internal audit approach, convention and methodology.

A suitably qualified person with appropriate experience and skills was appointed to the post of head of internal audit with effect from 1 August 2002. The internal audit directorate is currently staffed by two deputy-directors, a senior state accountant and a secretary. In the next financial year the capacity of the internal audit is to be strengthened so that a more effective service can be rendered to the department. With limited resources, the internal audit directorate has conducted several internal audits, special assignments as well as consulting assignments during the year under review.

Other governance structures

Management consultancy unit (MCU)

In addition to internal audit, the department established a management consultancy unit (MCU). This component is tasked mainly to monitor and assist with the performance of South Africa's missions abroad, which includes the optimal functioning of missions and the optimal utilisation of mission resources, including staff.

During the year under review, the MCU produced three reports on the reporting performance of missions. In addition, the MCU visited the following missions to evaluate their performance: Port Louis, Accra, Kuala Lumpur, London, Budapest, Warsaw, Lagos and Abuja. Comprehensive reports with findings, specific recommendations and action plans were compiled for each mission and submitted both to the business units and missions for implementation.

7. PROGRESS WITH FINANCIAL MANAGEMENT IMPROVEMENTS

A stable CFO infrastructure is now in place to facilitate a programme of financial management improvement initiatives in the department. With the PFMA espousing an approach of *management for results*, the following is part of a suite of initiatives that were introduced and is currently being implemented in a phased approach:

Decentralisation

"Let the manager manage" is a salient principle of the PFMA. The restructuring of the department in line with its strategic mandate took into account this principle and provided for the decentralisation of the corporate service function to branch level. The following are functional areas considered for decentralisation:

- Finance;
- Human resource administration;
- Provisioning; and
- Service centres.

Operational matters are being decentralised whilst policy co-ordination and liaison with outside stakeholders will continue to be administered centrally. In this regard, the business units are also responsible to manage their respective missions. Funds have been earmarked in the 2003/2004 financial year to operationalise corporate service decentralisation to branch level.

Financial systems

During the period under review, much effort was expended on the facilitation processes between the department and the State Information Technology Agency (SITA) for the appointment and consideration of a preferred service provider. The way is now clear for the department to implement an electronic financial system (on-line) at our missions. This will enable the department to fully comply with the reporting requirements of the PFMA.

It is also envisaged that the system will enable the department to comply with generally recognised accounting practice as the Accounting Standards Board and the National

Treasury migrate to full accrual accounting.

Normative measures for financial management

The department is committed to improving financial management and undertakes to monitor, on an on-going basis, the standards for financial management as developed by the National Treasury. Initiatives, which have been institutionalised since the implementation of the PFMA are:

- Financial training modules (PFMA, Treasury Regulations, budget and cash flow management and asset management) provided to officials.
- On-going review of departmental prescripts and policies aimed at improving the department's internal controls.
- Programme and responsibility managers (especially new ambassadors and heads of management to be deployed at our missions abroad) were provided with financial management training which included modules on the PFMA and Treasury Regulations, budgeting and cash flow management, procurement matters, financial processing guidelines, and asset and lease management issues.
- Key finance personnel have attended formal training in financial management (BAS, preparation of financial statements and budgets).
- Involved key role-players in the development of the department's strategic plan (2003-2005) and the production of the departmental MTEF for 2003-2005. Despite all the constraints, the department has endeavoured to comply with all financial legislation relating to reporting (accounting and budgetary) requirements.

8. PERFORMANCE INFORMATION

The department has developed its strategic plan for the next MTEF period, which articulates the strategic priorities of the department. The plan includes all statutory requirements as defined in chapter 5 of the PFMA and chapter 1, part III B of the new Public Service Regulations (2001).

To enhance service delivery and performance, measurable objectives, performance indicators and time frames have been developed.

Performance management system

The performance management and development system is a management tool for the effective translation of the departmental goals into actual deliverables in line with its mandate. A departmental policy on performance management has also been developed that is compliant with the regulatory framework that governs performance management at all levels in the public service.

It is an on-going process between the supervisor and the official that involves establishing clear targets and expectations, evaluating performance and taking constructive measures. All employees of the department are required to have a performance agreement.

Systems of implementation and monitoring

The minister, deputy-minister and director-general monitor the implementation of policy and the strategic plan by ambassadors at missions abroad and by senior officials of the department. Branches of the department and the programme managers at chief director level determine regional priorities and objectives, which are aligned to the department's strategic plan and priorities. Directorates and missions abroad implement business plans, which are country and region-specific. This operational level monitors implementation performance through a system of quarterly reports to head office on progress, supported by weekly and regular interaction and reports on the substance of the set objectives. The monitoring of progress and performance is further enhanced by the following systems:

- Head office business unit business plans and quarterly reports;
- Mission business plans and quarterly reports;
- Six-monthly reviews of the operating environment and priorities;
- A performance management system at all levels; and
- A departmental in-house six-monthly/annual strategic review.

These systems are further integrated and co-ordinated by a process of departmental management committees to ensure a coherent and focused approach.

9. NEW/PROPOSED ACTIVITIES

In June 2000 the department embarked on a process to secure a new head office premises. In consultation with the Department of Public Works a professional team was put together from various sectors to compile a feasibility study and to propose various options open to the department for acquiring a building. Of the various financial models investigated and after extensive analysis, the Public Private Partnership (PPP) model emerged as being the most suitable option. The main criteria against which these options were measured were affordability, value for money and the transfer of risk to the private party.

The feasibility study confirmed that the existing land owned by the department would not be sufficient to cater for the required space and that additional land would need to be acquired. A suitable government owned site has been identified and reserved for this purpose and cabinet approval has been granted to procure the building through the PPP process.

During the 2003/04 financial year, the appointment of a lead transaction advisor and departmental project officer will be finalised. A feasibility study will be conducted and the process of identifying and selecting a service provider will be finalised. The estimated completion date for the project is November 2006.

10. PAYABLES – CURRENT

The amount of R410,013 million included under payables relates to the inter-departmental suspense account (foreign currency system (FCS)/FMS interface). It represents the double entry (interface) of all transactions processed in foreign currencies. This account is cleared by means of a departmental transfer between the Rand and foreign currency Paymaster-General account. As soon as an accounting month is closed off on the FCS, a payment advice is completed which debits this account and clears it off. The balance is due to a timing difference, as the amount will be cleared in the next financial year.

11. RECEIVABLES

The bulk of the amounts owing by other departments relate to foreign allowances and accommodation expenses in respect of employees of partner departments. In this regard, the department incurs the expenditure on a recoverable basis. However, due to the lack of on-line financial systems, the department is facing difficulties to forward claims to partner departments on a monthly basis. This situation severely impacts on the cash-flow management of the department. During the year under review, the department has put numerous processes in place to deal with the situation as shown by the decrease of the outstanding amount from R274 million to R175 million.

However, it is important to report that despite management's proactive efforts in the expeditious settlement of inter-departmental claims, by establishing a process to deal with disputed amounts, it is disheartening to note that this matter has not yielded the desired results.

This is a challenge which the department pledges to tackle with greater vigour in the next financial year. Alternate strategies will be explored to deal with the issue to the satisfaction of all stakeholders (including users and taxpayers who examine annual financial statements to measure departmental performance).

12. CONTINGENCY LIABILITIES

Housing and motor finance guarantees

This relates to the financial guarantees made to commercial banks in respect of employees when they purchase a dwelling or a vehicle in terms of the housing policy or motor finance scheme. In the event that an employee fails to meet his/her obligations to the bank, the department either deducts the amount in instalments from that employee's salary or against his/her pension. In addition, if the employee resigns from the service, the department notifies the bank concerned and terminates the guarantee.

Financial guarantees

The Department of Water Affairs and the Lesotho Highlands Development Authority, through the Departments of Foreign Affairs of the respective countries, entered into a water treaty agreement in terms of which the Lesotho Highlands Development Authority was to supply water to South Africa.

In order for the Lesotho Highlands Development Authority to meet this challenge, it had to improve its infrastructure. They then applied for a loan from the Development Bank of South Africa. As part of the agreement, the department stood surety for the loan. It is important to report that all the repayments have been kept up to date.

Possible disputed agency services claims

This refers to amounts owed by various national and provincial departments in respect of agency services. The department embarked on a collection drive and some departments disputed the amounts owed. Although the department has an agreed process with the departments to verify the debts, it would be prudent to make a provision, as other departments may in some cases be proved to be correct. Although a provision of R50 million was made it is important to report that other departments were only able to confirm R23 million of the total outstanding amount of R175 million. Technically R152 million should therefore be regarded as claims in dispute. However, an amount of R50 million included in the total of R175 million represents the March 2003 claims, which were not submitted to other departments before year-end.

Approval

The financial position of the department as at 31 March 2003 and the results of its operations are set out in the attached financial statements:

- Appropriation statement
- Notes to the appropriation statement
- Income statement
- Balance sheet
- Statement of changes in net assets/equity
- Cash flow statement
- Notes to the annual financial statements
- Disclosure notes to the annual financial statements
- Statement of financial guarantees – Annexure 1
- Physical assets movement schedule – Annexure 2
- Intangible asset movement schedule – Annexure 3

The above-mentioned financial statements set out on pages 19 to 48 have been approved by the accounting officer.

Abdul S. Minty

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AS Minty

Acting Director-General:

Department of Foreign Affairs

31/05/2003

REPORT OF THE AUDITOR-GENERAL TO PARLIAMENT ON THE FINANCIAL STATEMENTS OF THE DEPARTMENT OF FOREIGN AFFAIRS – VOTE 3 FOR THE YEAR ENDED 31 MARCH 2003

1. AUDIT ASSIGNMENT

The financial statements as set out on pages 19 to 48, for the year ended 31 March 2003, have been audited in terms of section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996), read with sections 3 and 5 of the Auditor-General Act, 1995 (Act No. 12 of 1995). These financial statements, the maintenance of effective control measures and compliance with relevant laws and regulations are the responsibility of the accounting officer. My responsibility is to express an opinion on these financial statements, based on the audit.

2. NATURE AND SCOPE

The audit was conducted in accordance with Statements of South African Auditing Standards. Those standards require that I plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement.

An audit includes:

- examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements,
- assessing the accounting principles used and significant estimates made by management, and
- evaluating the overall financial statement presentation.

Furthermore, an audit includes an examination, on a test basis, of evidence supporting compliance in all material respects with the relevant laws and regulations, which came to my attention and are applicable to financial matters.

I believe that the audit provides a reasonable basis for my opinion.

3. AUDIT OPINION

In my opinion, the financial statements fairly present, in all material respects, the financial position of the Department of Foreign

Affairs at 31 March 2003 and the results of its operations and cash flows for the year then ended in accordance with prescribed accounting practice and in the manner required by the Public Finance Management Act, 1999 (Act No. 1 of 1999), as amended.

4. EMPHASIS OF MATTER

Without qualifying the audit opinion expressed above, attention is drawn to the following.

4.1 Receivables - interdepartmental balances

As reported in the previous audit report and disclosed in paragraphs 11 and 12 of the management report and notes 15.1 and 25 to the financial statements, the Department of Foreign Affairs (department) made provision for an amount of R50 million in respect of possible disputed agency services claims. Confirmations received from some of the departments indicated that the differences might be in excess of R150 million (2001/02: R150 million) on interdepartmental balances disclosed on their financial statements. The total amount of differences is unknown. The department had continued with its efforts to resolve the amounts owing by the other departments and the agreed-upon process to verify the disputed amounts.

4.2 Receivables – African Renaissance and International Co-operation Fund

According to note 15.3 to the financial statements, receivables include an amount of R29 861 680 in respect of the Africa Cup of Nations. The department effected these payments through a suspense account to the Mali Trust for the 23rd Africa Cup of Nations, on behalf of the African Renaissance and International Co-operation Fund. However, these payments had not been made in accordance with the requirements of section 5 of the African Renaissance and International Co-operation Fund Act, 2000 (Act No. 51 of 2000) and require, *inter alia*, regularisation by the Advisory Committee and the Minister of Finance.

4.3 Unauthorised expenditure

The department overspent its operational budget by R6.9

million as reflected under Programme 3: Public Diplomacy and Protocol. The expenditure is regarded as unauthorised in accordance with the Public Finance Management Act of 1999. Specific disclosure was not made in the notes to the financial statements in this regard nor was it allocated against unauthorised expenditure due to the closure of the Financial Management System. The department reported that the transaction would be processed in the next financial period.

5. APPRECIATION

The assistance rendered by the staff of the Department of Foreign Affairs during the audit is sincerely appreciated.

S A Fakie

Auditor-General

PRETORIA

30 July 2003

STATEMENT OF ACCOUNTING POLICIES AND RELATED MATTERS FOR THE YEAR ENDED 31 MARCH 2003

The financial statements have been prepared in accordance with the following policies, which have been applied consistently in all material respects, unless otherwise indicated. However, where appropriate and meaningful, additional information has been disclosed to enhance the usefulness of the financial statements and to comply with the statutory requirements of the Public Finance Management Act, 1999 (Act No. 1 of 1999 as amended) (act), the Treasury Regulations for Departments and Constitutional Institutions issued in terms of the act and the Division of Revenue Act, 2002 (Act No. 5 of 2002).

1. BASIS OF PREPARATION

The financial statements have been prepared on a modified cash basis of accounting, except where stated otherwise. The reporting entity is in transition from reporting on a cash basis of accounting to reporting on an accrual basis of accounting. Under the cash basis of accounting transactions and other events are recognised when cash is received or paid. Under the accrual basis of accounting transactions and other events are recognised when incurred and not when cash is received or paid.

2. REVENUE

Voted funds are the amounts appropriated to the department in accordance with the final budget known as the Adjusted Estimates of National Expenditure. Unexpended voted funds are surrendered to the National Revenue Fund.

Interest and dividends received are recognised upon receipt of the funds, and no accrual is made for interest or dividends receivable from the last receipt date to the end of the reporting period. They are recognised as revenue in the financial statements of the department and then transferred to the National Revenue Fund.

3. DONOR AID

Donor aid is recognised in the income statement in accordance with the cash basis of accounting.

4. CURRENT EXPENDITURE

Current expenditure is recognised in the income statement when the payment is made.

5. UNAUTHORISED, IRREGULAR, AND FRUITLESS AND WASTEFUL EXPENDITURE

Unauthorised expenditure means:

The overspending of a vote or a main division within a vote, or expenditure that was not made in accordance with the purpose of a vote or, in the case of a main division, not in accordance with the purpose of the main division.

Unauthorised expenditure is treated as a current asset in the balance sheet until such expenditure is recovered from a third party or funded from future voted funds.

Irregular expenditure means expenditure, other than unauthorised expenditure, incurred in contravention of or not in accordance with a requirement of any applicable legislation, including:

- the Public Finance Management Act,
- the State Tender Board Act, or any regulations made in terms of this act, or any provincial legislation providing for procurement procedures in that provincial government.

Irregular expenditure is treated as expenditure in the income statement.

Fruitless and wasteful expenditure means expenditure that was made in vain and would have been avoided had reasonable care been exercised. Fruitless and wasteful expenditure must be recovered from the official (a debtor account should be raised), or the vote if responsibility cannot be determined.

6. DEBTS WRITTEN OFF

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

7. CAPITAL EXPENDITURE

Expenditure for physical items on hand on 31 March 2003 to be consumed in the following financial year, is written off in full when they are received and are accounted for as expenditure in the income statement. Physical assets (fixed assets and movable assets) acquired are expensed, i.e. written off in the income statement when the payment is made.

8. RECEIVABLES

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

9. PAYABLES

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

10. PROVISIONS

A provision is a liability of uncertain timing or amount. Provisions are not normally recognised under the cash basis of accounting, but are disclosed separately in the notes to enhance the usefulness of the financial statements.

11. LEASE COMMITMENTS

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

12. ACCRUALS

This amount represents goods/services that have been delivered, but no invoice has been received from the supplier at year-end, or where the goods/services have been delivered, and an invoice is on hand but remains unpaid at year-end. These amounts are not recognised in the balance sheet as a liability or as expenditure in the income statement as the financial statements are prepared on a cash basis of accounting, but are however disclosed.

13. EMPLOYEE BENEFITS

Short-term employee benefits

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

Termination benefits

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

Retirement benefits

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

Medical benefits

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

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

14. CAPITALISATION RESERVE

The capitalisation reserve represents an amount equal to the value of the investments and/or loans capitalised, or deposits paid on behalf of employees at foreign missions before 31 March 2003. On disposal, repayment or recovery, such amounts are transferable to the Revenue Fund.

15. RECOVERABLE REVENUE

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

16. COMPARATIVE FIGURES

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

17. EXPENDITURE ABROAD IN FOREIGN CURRENCY

For expenditure incurred for missions abroad, the Rand value of cost is determined by the spot rate of exchange upon transfer of funds and the cost incurred in foreign currency. Mission cashbook balances are re-valued using daily spot rate of exchange upon each transfer of funds.