

INTERNAL AUDIT FRAMEWORK



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1. PURPOSE OF POLICY

The purpose of this Framework is to establish a minimum guideline for the development and operation of internal auditing in the Public Service. This Framework serves as a source of reference and it is the pre-eminent guidance mechanism on internal auditing in the Public Service. It is intended to ensure that Internal Audit Activities (IAA) comply with the requirements of:

- (i) The constitution of the Republic of South Africa;
- (ii) The Public Finance Management Act, 1999 as amended (PFMA)
- (iii) The Treasury Regulations (TR) issued in terms of the PFMA;
- (iv) The Municipality Finance Management Act (MFMA);
- (v) The Institute of Internal Auditors' (IIA) International Standards for the Professional Practice of Internal Auditing (ISPPIA);
- (vi) The corporate government principles as envisaged in the King Report on Corporate Governance in South Africa; and
- (vii) The COSO framework on internal controls, as well as the risk management framework.

Against this background, the Framework aims to provide a standard set of guidelines regarding internal auditing in Government. Research and findings of assessments conducted in the past indicated various levels of internal auditing practices within all facets of Government. The OAG believes that the Framework will set the tone and create the necessary impetus for a sustainable and effective internal auditing mechanism in government. This Framework is not meant to be prescriptive and should enhance the quality and standard of public sector auditing.

2. OBJECTIVE OF POLICY

The office of the Accountant- General (OAG), a division within National Treasury developed the Internal Audit (IA) Framework during the 2003/04 financial year. The Framework derives its mandate from the two legislations namely, the Public Finance Management Act, (Act no. 29 of 1999), and the Municipality Finance

Management Act, (Act No 56 of 2003) (MFMA). The OAG received requests from internal auditors in the Public Service for the framework to be updated. The update of the Framework is in view of the following:

- (I) Input received from various users needed to be incorporated into the Framework to increase its relevance and user friendliness in general;
- (II) The Framework needed to be updated to reflect developments in the discipline of internal audit;
- (III) The Framework needed to be expanded to include practical implementation guidelines that relate to the different spheres of government;

'Ready to use' standard documents and templates needed to be developed to support the ease of implementation; and, Best practices identified by the OAG needed to be incorporated into the Framework.

The reviewed Framework is intended to, amongst others be simple for users to understand; be Public Service specific and meet the specific requirements of the various spheres of government; and well-structured and easy to navigate.

3. SCOPE

The scope of internal audit activity embraces the wider concepts of corporate governance and risk – recognising that control exists in an organisation to manage risk and promote effective governance. The two types of internal audit services contemplated by the definition have been defined by the IIA as follows:

- (i) Assurance Services – an objective examination of evidence for the purpose of providing an independent assessment of risk management, control or governance processes for the organisation.
- (ii) Consulting Services – advisory and related client activities, the nature and scope of which are agreed upon with the client and which are intended to add value and improve an organisation's operations.

Throughout this document all references to "internal audit" will encompass both of these services.

4. POLICY DEFINITION

"Accounting Officer-AO" means the Municipal Manager, referred to in section 60 of the Act

“Act”	means the Municipal Finance Management Act 56 of 2003 as amended
“Committee”	means the Audit Committee and Performance Audit Committee established in terms of Section 166 of the Act
“Chief Financial Officer”	means the employee designated in terms of section 80(2)(a) of the Act
“Local Municipality”	means a municipality that shares municipal executive and legislative authority in its area with a district municipality within whose area it falls, and which is described in section 155(1)(b) of the Constitution of the Republic of South Africa, 1996 as a category B municipality
“Employee”	means a person in the employ of the Local Municipality as defined by section 213 of the Labour Relations Act 66 of 1995
“External Auditors”	means the Auditor-General as established in terms of section 188 of the Constitution of the Republic of South Africa, 1996
“Internal Audit Function”	means an outsourced or co-sourced service provider or internal appointed audit staff
“AC”	Audit Committee
“IA”	Internal Audit

5. LEGISLATIVE FRAMEWORK

A number of pieces of legislations have been, or are in the process of being, enacted by the government. It is important that both the organisation/municipality and the IAA have at least a basic understanding of the requirements of these legislations, provided in summary below. The same legislations mandate the establishment of the internal audit into the organisation/municipalities

- (i) The constitution of the Republic of South Africa;
- (ii) The Public Finance Management Act, 1999 as amended (PFMA)
- (iii) The Treasury Regulations (TR) issued in terms of the PFMA;
- (iv) The Municipality Finance Management Act (MFMA);
- (v) The Institute of Internal Auditors' (IIA) International Standards for the Professional Practice of Internal Auditing (ISPPIA);
- (vi) The corporate government principles as envisaged in the King Report on Corporate Governance in South Africa; and
- (vii) The COSO framework on internal controls, as well as the risk management framework.

6. POLICY OR PROCEDURE TARGET

6.1 Internal Audit Framework has been developed to highlight the overall process and functioning and the expected outcomes of Internal Auditing within the organisation and how it will assist the organisation to achieve its objectives through internal controls and risk management

6.2 The Policy is established to give guidance in the unit of the Internal Auditing in the municipality

6.3 All municipalities are expected to adopt this framework and customise it as per their capacity.

6.4 Treasury department are the custodian of this policy through the Accountant General Office.

7. GENERAL POLICY PROVISIONS

7.1 The purpose of this Internal Audit Framework is to communicate the progress made and the results on its implementation to the Audit Committee, Council and the management of the municipality.

7.2 The Internal Audit Framework has been developed and reviewed for the sole and exclusive use by the Mbhashe Local Municipality (council and management).

7.3 It may not be made available to anyone other than authorised persons within the Mbhashe Local Municipality or relied upon by any third party.

7.4 It should not be used for any other purposes for which it was not specifically scoped or designed, and as such, it should not be relied upon as evidence in any disciplinary proceedings involving employees, whether conducted internally or externally.

8. PROCEDURES FOR IMPLEMENTING POLICY

For the effective implementation of the Internal Audit Framework, all the necessary steps were followed during implementation:

8.1 Consultation of all the relevant stakeholders

8.2 Obligation of the framework

8.3 Realistic of the framework

8.4 Publicise of the framework

8.5 Training of the relevant staff to the framework

8.6 Consistent implementation of the framework and

8.7 Periodically review of the framework

9. OTHER INTERNATIONAL GUIDANCE

9.1 ISPPIA and Code of Ethics

The IIA has developed ISPPIA which are prescribed for applications to all its members and member organizations. These standards consist of three categories: the Attribute, Performance and Implementation Standards. The Standards should be applied in conjunction with the Code of Ethics.

9.2 The Committee of Sponsoring Organisation (COSO) / Tread-way Commission

COSO issued the Internal Control – Integrated Framework to help businesses and other organizations assess and enhance their internal control systems. This framework has since been incorporated into policies, rules and regulations, and used by thousands of enterprises to better control their activities in moving towards achievement of their established objectives.

9.3 Criteria of Control (COCO)

The CoCo was the initiative of the Canadian Institute of Chartered Accountants to strengthen control and governance. According to CoCo the essence of control in any organization is a combination of the organisation's purpose, commitment, and capability, monitoring and learning.

In CoCo, control is all the elements of an organization that, taken together, support people in the achievement of the organisation's objectives. The elements include resources, systems, process, culture, structure and tasks. Review of control means of review of all these elements and how they are inter-related and aligned with objectives.

10.AUDIT COMMITTEE

10.1 Introduction

The AC is an independent governance structure whose function is to provide oversight role on the system of internal control, risk management, and governance. Governance entails how an organization is managed, which includes culture, policies, strategies, and the way it deals with stakeholders as the AC.

10.2 Legal framework

Section 76(4) (d) of the PFMA states that the National Treasury may make regulations or may issue instructions concerning audit committees, their appointment and their functioning.

Section 77 of PFMA and 166 of MFMA provide for the establishment, composition and frequency of meetings.

10.3 The Audit Committee Charter

The purpose, roles, responsibilities and authority should be clearly documented in a charter. In the case of National and Provincial departments the charter should be accepted by the AC and approved by the AO in consultation with the Executive Authority (EA). In relation to municipalities the AO in consultation with Council should approve the AC charter. With regard to Public and municipal Entities the AC charter should be approved by the Board of Directors.

10.3.1 The AC's roles and responsibilities

(1) Determining the roles and responsibilities

The roles and responsibilities of an AC should be determined by the AO in consultation with the EA taking into account the following:

- (i) The organisation's size, complexity and nature of its business;
- (ii) Nature governance structure;
- (iii) Maturity of organisation's risk and control environment;
- (iv) Skills, experience and personal qualities of potential members; and
- (v) Mechanisms and process which need to be established to enable the committee to meet its responsibilities.

(2) Risk Management

Risk management is an essential part of effective corporate governance and whilst it is a management responsibility, management expects the AC to oversee and provide advice on the organization's risk management. The AC needs to review:

- (i) Whether management has a comprehensive risk management framework;
- (ii) Whether a sound and effective approach has been followed in developing strategic risk management plans;
- (iii) The impact of the organisation's risk management framework on the control environment; and
- (iv) The organisation's fraud prevention plan to be satisfied that the organization has appropriate processes and systems in place to capture, monitor and effectively investigate fraudulent activities.

(3) Control Framework

The AC members need to have a good understanding of the control framework. This understanding will enable the AC to evaluate the adequacy of the organisation's control environment and will be a basis from which reasonable assurance can be provided that the organisation's objectives and goals will be achieved efficiently and economically.

(4) Internal Audit

IAA should be a major source of information to the AC on the performance of the organization. To maximize the value of IAA, it is important that open lines of communication are established and maintained between the IAA and AC.

The AC's responsibilities in relation to IAA should be as follows:

- (i) Act as a forum for communication between management, internal and external audit;
- (ii) Review the IA Strategic and Operational plans are based on the organisation's risk assessment, and recommended approval of them by the AO;
- (iii) Advise the AO on the adequacy of IA resources needed to carry out auditing responsibilities, including the completion of the approved IA plan;

- (iv) Oversee the co-ordination of audit programs conducted by internal and external audit;
- (v) Review all audit reports and provide advice to the AO on significant issues identified in audit reports and action taken on issues raised;
- (vi) Monitor management's implementation of IAA recommendations;
- (vii) Review the IA Charter to ensure that appropriate organizational structure, authority, access and reporting arrangements are in place;
- (viii) Periodically review the performance of the IAA; and
- (ix) Provide advice to AO on the appointment and dismissal of the CAE.

(5) External Audit

The AC will have valuable insight into the effectiveness of the organisation's risk, control, financial reporting, operational reporting and legislative framework if a good relationship exists with external audit.

The AC's responsibilities in relation to external audit should be as follows:

- (i) Provide input and feedback on the financial statements and audit coverage proposed by external audit and provide feedback on the audit services provided;
- (ii) Review all external audit plans and monitor management's implementation of audit recommendations.
- (iii) Provide advice to the AO on action taken on significant issues raised in external audits; and
- (iv) Review external audit costs.

10.3.2 Composition and Membership

(a) Composition

Section 166 (4) of the MFMA states that an AC must consist of at least three persons of whom the majority may not be in the employ of the department or municipality. The majority of members should be financially literate and qualified. The appointment must be done by the AO in consultation with the EA or Council. The appointment members should enter into contract with the organization.

The size of the AC should be influenced by the nature and extent of its responsibilities as covered in the charter.

10.3.3 Qualities

In determining the composition of the AC, the AO should look for the following qualities:

- (i) The ability to conduct responsibilities in the context of the organisation's strategic objectives and overall corporate governance of the organization;
- (ii) The ability to act independently and be proactive in advising the AO of issues that require further management attention;
- (iii) The ability to ask relevant questions, evaluate the answers and continue to probe for information until completely with answers provided;
- (iv) Independence;
- (v) A professional approach to duties, including commitment of time and effort;
- (vi) The ability to encourage openness and transparency; and
- (vii) The ability to work constructively with management.

10.3.4 Skills and experience

Members should be selected from different areas of expertise to enhance the AC's overall knowledge of the organization. The appointed members should collectively possess the following:

- (i) Broad business, corporate governance and/or financial management experience;
- (ii) Public sector experience;
- (iii) An understanding of the business in which the organization operates;
- (iv) Familiarity with risk management practices;
- (v) An understanding of internal controls;
- (vi) An understanding of major accounting practices and public sector reporting formats;
- (vii) Familiarity with legislative requirements; and
- (viii) Understanding of the roles of internal and external audit.

10.3.5 Independence of members

In order to be effective, the AC needs to operate independently of line management and it needs to bring objectivity to the deliberations. To enhance the AC's independence, it is recommended that:

- (i) The majority of AC members should be independent of the organization and should preferably not be in the public service;
- (ii) The appointment of AC members who exhibit an independence of mind in their deliberations; and
- (iii) AC members should not serve more than two consecutive terms.

10.3.6 Appointment of Chairperson

One of the AC members should be appointed the chairperson. The AO should appoint the chairperson in consultation with the executive authority. The chairperson should be an independent member not in the employ of the organization. The following factors should be considered in appointing the chairperson:

- (i) The personal qualities and abilities to lead discussions;
- (ii) Encouragement of other members to participate in AC meetings; and
- (iii) Conducting meetings in a manner that demonstrates a desire to establish effective communications with all stakeholders.

10.3.7 Term of office

The chairperson should be appointed for a minimum of between two and three years to ensure that he/she contributes most effectively and provides stability to the AC. AC members should be recruited to introduce new perspectives and thinking to AC discussions. Rotation is encouraged as it enhances the independence of the AC.

Members should serve at least a minimum of three years with an option to renew the contract. Recruitment should be staggered to prevent a loss of knowledge and skills base of members at one time. Members should be encouraged not to terminate their contracts until they have shared their experience with new members.

10.3.8 Induction of members

A formal process of induction should be in place. This process should provide new members with sufficient briefing and information to understand their responsibilities and management expectation about their role and performance. The new members should meet and be briefed by the AO and chairperson of the AC should be introduced to the CAE and the external auditors.

Information to be provided to new members should include:

- (i) The organisation's governance structure and how the AC operates within this structure;
- (ii) A copy of the AC charter and recent AC minutes including details of outstanding issues;
- (iii) Copies of the relevant legislation;
- (iv) Copies of the organisation's annual report, strategic plan, code of conduct and risk management plans;
- (v) A briefing from management and IA on the risk, control and governance processes; and
- (vi) A copy of the IA Charter, annual work plan and recent audit reports.

The chairperson in consultation with the AO should identify opportunities for further education of the members in arrears of risk management, financial reporting and corporate governance. This may take a number of forms:

- (i) Attendance of seminars or courses;
- (ii) Provision of relevant written material;
- (iii) Presentation by senior management; and
- (iv) Discussion and presentation from internal and external audit.

An AC should have the following characteristics:

- (i) A good understanding of the committee's position in the governance structure;
- (ii) Clearly defined roles and responsibilities;
- (iii) Members with relevant personal qualities, skills and experience;
- (iv) The ability to maintain effective relationships with key stakeholders;
- (v) The ability and capacity to conduct its affairs efficiently and effectively; and

11. ESTABLISHMENT OF IAA

Background

Section 38 (1) (a) (ii) and 76 (4) of the PFMA, Section 165 of the MFMA and King iv define the role and responsibilities of IA.

IA is an important component of internal control, risk management and corporate governance and provides the necessary assurance and advisory services to the organization.

IA is one of the most significant management tools and can provide value-added services to the organization. When objectively and adequately resourced, an IAA should be in a position to provide management with much of the assurance it requires regarding the effectiveness of the system of internal control, risk management and governance processes. The IAA must be well planned, organized, staffed, directed and monitored.

IA must be conducted in accordance with the standard set by the IIA. These standards together with the various Practice Advisories issued by the IIA should provide much of the guidance required by IAA for conducting their work.

11.1 Planning

11.1.1 Identifying the CAE

The CAE's role is to provide advice, counsel, and opinions regarding the organization's efficiency and effectiveness in risk management, internal control and corporate governance.

To be effective in this role, the CAE should be someone who can be viewed and accepted as a member of the organisation's senior management team.

The CAE should at least possess the following qualifications;

- (i) Post graduate degree in Auditing and/or Accounting;
- (ii) Professional designation such as Certified Internal Auditor (CIA) and other IIA designations; and
- (iii) Other professional designations such as Chartered Accountants (CA)

The incumbent should preferably have following experience and qualities;

- (i) At least five (5) years in internal audit management experience;
- (ii) Membership of the IIA
- (iii) High level of personal and professional ethics; and
- (iv) An understanding of the risk management processes and practices.

11.2 Accountability, Independence and Objectivity

11.2.1 Accountability

The CAE must report to a level within the organization that allows the IAA to fulfill its responsibilities. The level must have sufficient authority to promote independence and to ensure broad coverage, adequate consideration of engagement communications, and appropriate action on engagement recommendations.

The CAE should report functionally to the AC, and administratively to the AO of the organization to:

- (i) Assist the AO by providing periodical assessment on the adequacy and effectiveness of the organisation's process for controlling its activities.
- (ii) Report significant issues related to the process for controlling the activities of the organization, including potential improvement to those processes, and
- (iii) Periodically provide information on the status and results of the annual IS plan and the sufficiency of the IAA's resources.

11.3 Independence

Independence is achieved through the organization status and the objectivity of IAA. IAA is independent when they can carry out their work free and objectively.

- (i) IAA should have the support of senior management and of the AC so that they can gain the co-operation of the audit client and perform their work free from interference.

- (ii) The CAE should have direct communication with the relevant EA, AO, AC, or other appropriate governing authority.
- (iii) Direct communication occurs when the CAE regularly attends and participates in meetings of the relevant EA, AC and appropriate governing authority which relate to its oversight responsibilities for auditing, financial reporting, corporate governance and control.
- (iv) The attendance and participation of CAE at these meetings provide an opportunity to exchange information concerning the plans and activities of the IAA.

Independence is enhanced when the AC concurs in the appointment or removal of the CAE.

11.4 Additionally, the IAA should

- (i) Have no direct operational responsibility or authority over any of the activities they review;
- (ii) Not develop nor install systems or procedures, prepare records, or engage in any other activity that would normally be audited;
- (iii) Not initiate or approve accounting transactions external to the IAA; and
- (iv) Implement a control to ensure that each audit project team member should declare interest before commencement of an audit project.

11.5 Objectivity

Each internal auditor should have an objective attitude and should be in a sufficiently independent position to be able to exercise judgment, express opinions and present recommendations with impartiality.

11.5.1 Specifically:

- (i) An internal Auditor should be free from any conflict of interest arising from professional or personal relationships or other interest which he/she may be subject to audit, and

- (ii) An Internal Auditor should be free from undue influence which restricts or modifies the scope of the audit work, or significantly affects judgement regarding the contents of any audit report.

11.5.2 The internal Audit Charter

An IA charter serves as the IAA statement of purpose, authority and responsibility, and must be in writing and address the following:

- (i) The IAA's purpose, authority and responsibility;
- (ii) The standard to comply with;
- (iii) The scope of work to be undertaken;
- (iv) The position of the IAA within the organization;
- (v) The description of assurance and nature of consulting activities;
- (vi) The period of review of the charter;
- (vii) The appointment and dismissal of the CAE; and
- (viii) Access to information, properties and people

The IA Charter must be approved by the chairperson of the AC and accepted by the AO.

11.5.3 Organizing the IAA

11.5.3.1 planning

- (a) The CAE needs to direct, supervise and manage the activities of IAA.
- (b) These include amongst others planning, resource management, implementation of operating policies and procedure, review of work, coordination of assurance activities and quality assurance.

11.5.3.2 The Audit Plan and Process

- (i) Audit planning should be based on an assessment of risk and exposure that may affect the organization and should be done at least annually in order to reflect the most current strategies and direction of the organization.

- (ii) The best way to add value to an organization is to make sure the risk assessment and the plan developed from the assessment reflect the overall objectives of the organization.
- (iii) A risk based audit plan ensures that audit activities effectively focused on those arrears where the risk of exposure is greatest.
- (iv) The CAE must ensure must ensure that a strategic plan and annual plan are developed annually and approved by the AC and the AO.

11.5.3.3 Developing an Internal Audit Strategic Plan

Developing a strategic audit plan follows a logical process as described below:

(a) Understanding (Step1)

A top-down view of the organization is taken to better understand the business and operational risks and the controls for managing those risks. This view depicts the environment within which each organization operates.

(b) Strategic overview (step 2)

To identify the risk to which the organization is currently exposed and those to which it is likely to be exposed in the future, an understanding of the strategic plan and objectives for the organization must be obtained. The strategic plan overview covers the following arrears:

- (i) Mission
- (ii) Vision
- (iii) Values, and
- (iv) Objectives.

Using the above information, a strategic risk workshop / interviews should be conducted where the risk that threaten the attainment of the organisation's strategic objectives are identified and analysed. The controls put in place to manage the risks should be identified.

(c) Detailed analysis (step 3)

The understanding of the strategic intent and the functioning of the organization are extended through a consideration of management's breakdown of the strategic objectives and intent into organization objectives and or / process specific objectives. A detailed risk analysis of the organization is conducted to identify those risks that impact on the achievement of objectives.

The analysis:

- (i) Assesses the impact of each risk on the objectives;
- (ii) It considers the relevant risk management activities applied to the risk;
- (iii) The effectiveness of such activities; and
- (iv) Looks at any action needed to improve the risk management activities.

In considering the effectiveness of risk management activities actual or perceived control, measures are identified and their effectiveness in regard to the identified risk as assessed.

(d) Consolidated risk reporting (step 4)

- (i) The reporting of the results provides detailed reports of the processes reviewed that allow for risk rating, control effectiveness evaluation, detailed action plans and audit strategy determination.
- (ii) Summary reports can be extracted that set out the risk management response per business process model or control criteria (for example – severity of risk of external factors, how well these risks are managed using what control criteria; for instance, commitment, measurement).
- (iii) The data can be used to plan and direct a risk management approach and provide the basis of risk management activities.

(e) Risk management activities (step 5)

- (i) Management is responsible for ensuring effective risk management in the organization.
- (ii) The approach followed provides a mechanism of formalising the responsibility and establishing accountability for management activities.

- (iii) This is often achieved through the establishment of a “Risk committee” function.
- (iv) Their efforts should identify further actions that may be needed to reduce risk to an unacceptable level, and should also identify where the control effectiveness assessments were not corrected, and update them accordingly.

11.5.4 Annual audit plan

The annual IA plan must be developed taking into account the results of the risk assessment and the associated strategic audit plan so as to:

- (i) Focus arrears of IA activities;
- (ii) Determine IA scope in relation to the schedule assignment;
- (iii) Determine the resources to the planned audit assignments;
- (iv) Establishing the timing of performance of the audit assignments; and
- (v) Determine the reporting requirements and deadlines.
- (vi) It must be in sufficient detail for the AO and management to understand the assignment’s purpose and scope.
- (vii) Management must be given the opportunity to formally review and comment on the annual IA plan.
- (viii) The annual IA plan should be reviewed to identify any amendment needed to reflect changing priorities and emerging audit needs. The AO and the AC should approve material changes to the audit plan.

11.5.5 Risk based planning

- (i) The CAE should establish risk-based plans to determine the priorities of the IAA, consistent with the organisation’s goals.
- (ii) This means that the IAA’s plans as well as the IAA field work must focus on the risks to which the organization is exposed.
- (iii) Best practice internal auditing also dictates that a specific strategy is developed, which best directs IAA efforts to where the organization needs it most, at any given time.

- (iv) This means that the correct balance of risk based versus cyclical based audits needs to be found. This balance depends on the maturity of an organisation's systems and processes, the extent to which policies and procedures (and hence internal controls) are entrenched and complied with, and the general strength of the wider control environment.
- (v) Best practice is that the IAA spends most of its time on risk-based audits, with the balance on cyclical based audits, follow-up audits and ad hoc requests.

11.5.5.1 Risk based audits

- (i) Given the results from the risk assessment performed which generally indicate only a satisfactory-to-weak control environment, it may be appropriate for the IAA to focus its attention on the high risk arrears but concentrate on ensuring that the key controls are in place and adhered to.
- (ii) This can be adjusted depending on the results from first audits, given that the audit plan is flexible, through management on AC approval.

11.5.5.2 Cyclical audits

- (i) IAA may decide to focus its attention on certain medium to lower risk arrears, for example to achieve general or specific improvements in the control environment or culture.
- (ii) These cyclical audits are normally conducted on a yearly basis with the aim of monitoring and maintaining (through the reports issued and taken) a sound internal control environment.

11.5.5.3 Ad hoc requests

- (i) IAA might consider ad-hoc request from management, but such requests should flow from the written authorized charter and with the approval of the AC.
- (ii) However before accepting these requests IAA should assess the request against the identified / planned audits of the high-risk areas and priorities

the request based on how much value can be added, comparatively, prior to deciding whether or not to accept the request.

In developing the annual IA plan the following key issues must be borne in mind:

- (i) Availability (capacity) and skills of IA staff;
- (ii) Changes in the risk environment of the organization – the risk environment should be assessed on an annual basis;
- (iii) Approval and acceptance of this plan by the AC;
- (iv) The materiality of ad-hoc requests – could have a significant impact on the normal audit planning and timing process.

11.5.6 Budget of IA

It is the responsibility of AO to ensure that the IAA is adequately resourced for effective functioning of the unit. The CAE should control and have responsibility over the IAA's budget.

The IAA's budget should at least cover the following items:

- (i) Infrastructure including accommodation, personnel related expenditure;
- (ii) Capital expenditure and software;
- (iii) Training and development;
- (iv) Membership fees; and
- (v) Quality assurance programs

11.5.7 Staffing

- (i) The CAE, in conjunction with the AO, should develop an IAA structure taking cognizance of the organization's needs including risk and complexity of the operations.
- (ii) Provision should be made for levels of supervision and review of audit work in line with due professional care as provided for the ISPPA.
- (iii) The CAE should develop a recruitment, placement, training and staff retention programme to ensure that appropriate skills should be placed on qualifications, skill and experience.

- (iv) To improve effectiveness of the IAA, staff at all levels should have well-documented job descriptions, clear goal setting, performance evaluation and training programmes.

11.5.8 Outsource or Co-Source of Staff

- (i) The IAA may be outsourced where the organization requires capacity to develop its internal capacity and is deemed to be feasible and /or cost effective.
- (ii) Where the IAA is outsourced, oversight and responsibility for the IAA cannot be outsourced.
- (iii) A senior official reporting to the head of the organization (preferable with an audit background) should be assigned responsibility for management of the outsourcing of the IAA.

Consideration for evaluating outsourcing alternatives:

- (i) Available resources: The organization may have sufficient resources (financial, physical, human etc) to establish an in-house IAA. Outsourcing is normally considered when it is feasible for the organization; and
- (ii) Size of the organization: Both large and small organization may need to take advantage of outsourcing alternatives. Common reasons include temporary staff shortages, specialty skills, special audit project work and supplementary staff to meet deadlines.

11.5.9 Quality Assurance

- (i) The activities of the IAA should be guided, monitored and supervised at each level of operation to ensure that they are consistently performed in accordance with the IAA's standards.
- (ii) The IAA should be subjected to a quality assurance review at least once every five years, the results of which should be communicated to the AC.

11.5.10 Internal reviews

The CAE should ensure that internal audit reviews are performed. These should ideally be conducted by senior officials who are experienced in the field. Internal reviews should appraise among others:

- (i) Compliance with the IAA charter;
- (ii) Compliance with the IAA methodology;
- (iii) Compliance with the IIA standards; and
- (iv) Achievements and performance standards/indicators, etc.

11.5.10 External reviews

- (i) External reviews should be conducted by a qualified reviewer or review team from outside the organization.
- (ii) The scope of the external audit assessments will, among others, cover matters related to independence and objectives of the IAA expressed by the senior management and AC, integration the IAA into the organisation's governance process, efficiency and effectiveness of approach, audit strategy and plans.
- (iii) On completion of the external assessment, the review team should issue a formal report containing an opinion on the level of the IAA's compliance with the ISPPIA. The CAE should prepare a written action plan in response to comments and recommendations in the report

11.5.11 Self-assessment with independent validation

- (i) An alternative to conduct external assessment if for the IAA to conduct a self-assessment with an independent external validation.
- (ii) This approach allows internal assessment to be performed and documented.
- (iii) The results of the self-assessment are presented to the independent validator for evaluation.

12. NATURE OF WORK

IAA should evaluate and contribute to the improvement of risk management, control and governance processes using a systematic and discipline approach.

12.1 Risk Management

- (i) IAA is responsible for providing assurance to management and the AC on the adequacy and effectiveness of the risk management process.
- (ii) Risk management is a key responsibility of the AO and management.
- (iii) Management should ensure that adequate risk management processes are in place and functioning as intended.

- (iv) IAA should assist management and the AC by examining, evaluating, reporting and recommending improvements on the adequacy and effectiveness of management's risk processes. Developing assessment and reports on the organisation's risk management process should be audit priority.
- (v) IAA must satisfy them that the organisation's risk management processes address five key objectives to formulate an opinion on the overall adequacy of the risk management processes.
- (vi) The five key objectives of risk management are:
 - (a) Risk arising from business strategies and activities should be identified and prioritized. These risks should focus on the efficient, economic and effective use of resources, as well as any duplications of functions that might exist;
 - (b) Management should determine the level of risk acceptable to the organization;
 - (c) Risk mitigation activities should be designed and implemented to reduce, or manage risk at level acceptable by management;
 - (d) Management should receive periodic report of the results of risk management processes; and
 - (e) Ongoing activities should be conducted to periodically reassess risk and the effectiveness of controls to manage risk.

12.2 Control

- (I) Before controls can be evaluated, management should determine the level of risk they are willing to accept in the area to be reviewed.
- (II) Controls in place can then be assessed to determine how successful they are expected to be in reducing risk to a desired level.

12.2.1 Types of Internal Controls

(a) Directive Controls

1. A directive control is intended to cause or encourage a desirable event to occur, for example orientation all new employees on organizational policies, and implementation of a delegation within the organization.

(b) Preventive Controls

1. A preventive control is designed to deter undesirable events from occurring.
2. Preventive controls include employment of trustworthy and competent people, segregation of duties, and physical control over assets to prevent improper conversion or use.

(c) Detective Controls

1. Detective controls are designed to detect undesirable events that have occurred.
2. Detective controls include reviews and comparison, such as records of performance and independence checks on performance.
3. They also include such control devices as bank reconciliations, cash counts, physical counts of inventories and analysis of variances, and computerized techniques such as transaction limits and passwords.

(d) Corrective Controls

1. Corrective controls rectify an error or irregularity which has been detected.
2. An example is causing an employee to pay back funds that were fraudulently acquired from the organization.

8.3 Evaluation of controls

8.3.1 Based on the results of the risk assessment the IAA must evaluate the adequacy and effectiveness of controls encompassing the organisation's governance, operations, and information systems. This should include:

- (i) Reliability and integrity of financial and operational information;
- (ii) Effectiveness and efficiency of operations;

- (iii) Safeguarding of assets; and
- (iv) Compliance with laws, regulations, and contracts.

8.3.2 IAA should perform sufficient audit work and gather information to form an opinion on the adequacy and effectiveness of the internal control process. The CAE must communicate the overall opinion on a timely basis.

The following aspects should be considered when assessing controls for adequacy:

- (a) The control environment and management attitude towards controls;
- (b) Standard control practices (generally accepted management practices); and
- (c) Compliance with other generally used control frameworks.

After satisfying oneself that the controls are adequate, the internal auditor should assess the controls for effectiveness.

To ensure that the correct conclusion are reached and supported by acceptable evidence the auditors are required to analyse and evaluate the findings of the execution of the audit in order to determine whether the controls are effective or not.

The auditor may reach one of the following conclusions when evaluating the controls for effectiveness:

12.3 Effective

The existing controls are effective, i.e. they provide reasonable assurance that the activity will achieve its performance.

13. INEFFECTIVE

The existing controls are ineffective, i.e. they do not provide reasonable assurance that the activity will achieve its performance objectives.

14. GOVERNANCE

The IAA must assess and make appropriate recommendations for improving the governance process in its accomplishment of the following objectives:

- (i) Promoting appropriate ethics and values within the organization;
- (ii) Ensuring effective organizational performance management and accountability;
- (iii) Communicating risk and control information to appropriate areas of the organization; and
- (iv) Coordinating the activities of and communicating information among the board, external and internal auditors, and management.

In promoting the ethics and values within an organization IAA should evaluate whether:

- (a) The organization has a formal code of conduct and other policies communicating appropriate ethical and moral behavioral standards and addressing acceptable operational practices and conflict of interest;
- (b) An ethical tone has been developed at the top and communicated throughout the organization;
- (c) High ethical standards are in place when dealing with the public, EA, employees, suppliers, auditors, and others;
- (d) Management cooperates with auditors and other evaluators, discloses known problems to them, and values their policies and procedures or violations of the code of conduct; and
- (e) The types of disciplinary actions that are taken are widely communicated throughout the organization so that others know that if they behave improperly, they will face similar consequences.

In ensuring efficient organizational performance and management accountability IAA should evaluate whether:

- Management has established overall organization-wide objectives in the form of mission, goals, and objectives in strategic and annual performance plans;
- The organization-wide objectives relate to and stem from program requirements established by legislation;
- The organization-wide objectives are specific, measurable achievable, realistic and timeous enough to clearly apply to the organization;
- Strategic plans support the organization-wide objectives; and
- The organization-wide objectives are effectively communicated to all employees.

15. REVIEWAL AND APPROVAL OF THE IA FRAMEWORK

The AC Committee shall annually, review the IA Framework, and determine its adequacy and effectiveness for current circumstances and recommend to Council for approval of any amendments that may be required

Compiled by:

Internal Audit Manager

(Mr A. Mtyhida)

Date

Recommended by:

Municipal Manager

(Mr M.Nako)

Date

Approved by:

Chairperson- on behalf of Audit Committee

(Mr S. Mxunyelwa)

Date