

THEMBISILE HANI LOCAL MUNICIPALITY



INTERNAL AUDIT CHARTER 2014/15

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1. INTRODUCTION

In terms of Section 165 (1) of the Municipal Finance Management Act 56 of 2003, the Act states that “each municipality and municipal entity must have an internal audit unit subject to subsection (3)”.

The Standards for the Professional Practice of Internal Auditing requires that the purpose, authority and responsibility of the Internal Audit function be formally defined in an internal audit charter, consistent with the Definition of Internal Auditing, the Code of Ethics, and the Standards.

2. PURPOSE OF THE INTERNAL AUDIT CHARTER

The purpose of this charter is to set out the nature, role, responsibility, status and authority of Internal Audit Unit and to also outline the scope of the audit work as conferred by the Municipal Manager (Accounting Officer) and Audit Committee to the Internal Audit, in terms of section 165 of Municipal Finance Management Act.

3. DEFINITION OF INTERNAL AUDIT & MANDATE

Internal audit is a strategic management tool. The Institute of Internal Audit defines internal auditing as: *“an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.”*

Internal Audit draws its mandate from the following legislations and regulations:

- 1) Section 165 of the Municipal Finance Management Act, No. 56 of 2003 which requires that the internal audit unit of a municipality:
 - Prepare a risk-based audit plan and an internal audit program for each financial year;
 - Advise the Accounting Officer and report to the Audit Committee on the implementation of the internal audit plan and matters relating to:-
 - i) internal audit;
 - ii) internal controls;
 - iii) accounting procedures and practices;
 - iv) risk and risk management;
 - v) performance management;
 - vi) loss control; and
 - vii) compliance with this Act, the annual Division of Revenue Act and any other applicable legislation; and
 - Perform such other duties as may be assigned to it by the Accounting Officer.

- 2) Section 45 of the Municipal Systems Act, 2000 & Regulation 14 (1) (a) of the Municipal Planning and Performance Management regulations, 2001 which requires that the results of performance measurements, be audited as part of the municipality's Internal Auditing processes.

The Internal Audit Unit has the responsibility to discuss the definition of Internal Audit with management on an annual basis.

4. OBJECTIVES AND SCOPE OF WORK

The primary objective of Internal Audit is to assist management and the Audit Committee to effectively discharge their responsibilities. To this end, Internal Audit promotes effective controls and provides an independent analysis, appraisals, recommendations, counsel and information concerning the activities reviewed with a view to improve accountability and performance using a risk based audit approach.

The scope of the Internal Audit work is to derive whether the Thembisile Hani Local Municipality's network of risk management, control and governance processes as designed and directed by management is adequate, effective and functioning in a manner to ensure that:

- Risks are appropriately identified, assessed and managed;
- Interaction with the various governance groups occurs as needed;
- Significant financial, managerial and operating information is accurate, relevant, reliable and timely;
- Employees' actions are in compliance with the municipal policies, standards, procedures, instructions, code of ethics and applicable laws, regulations and contractual obligations;
- Resources are acquired economically, used efficiently, and adequately protected and in accordance with the relevant laws and regulations;
- Programs, plans, and objectives are achieved;
- Quality and continuous improvement are fostered in the municipal control process; and
- Significant legislative or regulatory issues impacting the municipality are recognized and addressed appropriately.

The Internal Audit coverage may extend to all areas of the organization and include financial, accounting, administrative and other operational activities. The extent and frequency of internal audits shall depend upon varying circumstances such as results of previous audits, relative risks associated with activities, materiality, the adequacy of the systems of internal control, the resources available and budget allocations.

The internal auditors may identify opportunities for improvement of management control, service delivery, and the municipality's image. These shall be communicated to appropriate management.

5. ACCOUNTABILITY

The CAE in the discharge of his/her duties shall be accountable to management and the Audit Committee to:

- Provide annually an assessment on the adequacy and effectiveness of the municipality's processes for controlling its activities and managing its risks in the areas set forth in this charter.
- Report significant control issues, including potential improvements to those processes, and provide information concerning such issues for further action by management
- Periodically provide information on the status and results of the annual audit plan and the sufficiency of the organization resources.
- Coordinate with other control and monitoring functions (risk management, compliance, security, legal, ethics, environmental and external audit).
- Provide assurance on performance information generated by the municipality.

6. INDEPENDENCE AND OBJECTIVITY

6.1. ORGANIZATIONAL INDEPENDENCE

To provide and maintain the independence of the Internal Audit Activity (IAA), the CAE and the Internal Audit personnel shall report administratively to the Municipal Manager and functionally to the Audit Committee. Functional reporting means that the Audit Committee shall:

- Approve the charter of the internal audit function.
- Approve the internal audit risk-based audit plan.
- Receive communications from the CAE on the results of the internal audit activities or other matters that the CAE determines are necessary, including private meetings with the CAE without management present.
- Approve all decisions regarding the appointment or removal of the CAE.
- Make appropriate inquiries of management and the CAE to determine whether there are scope or budgetary limitations that impede the ability of the internal audit function to execute its responsibilities.

Internal Audit Activity shall have direct access to and/or communication with the Audit Committee or other appropriate governing authority.

Administrative reporting typically includes:

- Budgeting and management accounting.

- Human resource administration, including personnel evaluations and compensation.
- Internal communications and information flows.
- Administration of the organization's internal policies and procedures.

6.2. OBJECTIVITY

To maintain objectivity, the Internal Audit personnel shall not be involved in the day-to-day execution of control procedures for any unit of the municipality. If independence or objectivity is impaired in fact or appearance, the details of the impairment shall be disclosed to appropriate parties. The nature of the disclosure will depend on the impairment.

Internal audit shall report to the Audit committee any situations in which a conflict of interest or bias is present or may reasonably be inferred. Impairment to organizational independence and individual objectivity may include, but is not limited to, personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations, such as funding.

A scope limitation is a restriction placed upon the internal audit activity that precludes the audit activity from accomplishing its objectives and plans. Among other things, a scope limitation may restrict the:

- Scope defined in the charter.
- Internal audit activity' access to records, personnel, and physical properties relevant to the performance of engagement.
- Approved engagement work schedule.
- Performance of necessary engagement procedures.
- Approved staffing plan and financial budget.

A scope limitation along with its potential effect shall be communicated preferably in writing to the Audit Committee, management or other appropriate governing authority

7. STATEMENT OF RESPONSIBILITIES

7.1. INTERNAL AUDIT

The CAE and the Internal Audit staff have inter alia the responsibility to, but not limited to:

- Develop a strategic and flexible annual audit plan using appropriate risk-based methodology, including any risks or control concerns identified by management and submit the plan to the Audit Committee for review and approval;
- Implement the annual audit plan, as approved, including, and as appropriate, any special tasks or projects requested by management and the Audit Committee;

- Establish policies and procedures to guide the IAA and direct its administrative functions;
- Maintain a professional audit staff with sufficient knowledge, skills, experience and professional certifications to meet the requirements of this charter;
- Establish a quality assurance program by which the CAE assures the operation of internal auditing activities;
- Perform consulting services, beyond internal auditing's assurance services, to assist management in meeting its objectives;
- Issue at least quarterly reports to the Audit Committee and management summarizing results of audit activities; and
- Appropriately consider the scope of work of other independent assurance providers such as external auditors and regulators for the purpose of providing optimal audit coverage to the organization at a reasonable overall cost and preventing any duplication of audit efforts.

7.2. MANAGEMENT

Management of the municipality has responsibility to, but not limited to:

- Ensure that proper internal control mechanisms exist and are enforced.
- Co-operate and participate in the development of audit scope for every audit engagement.
- Provide all relevant documents and information in whichever form required by the internal auditors for the performance of the audit engagements.
- Provide the necessary co-operation and assistance as mutually agreed upon during the audit engagement.
- Respond timely to audit requests and audit findings; and implement audit recommendations.

7.3. RESPONSIBILITY FOR DETECTING AND REPORTING IRREGULARITIES

The Internal Audit Unit is not legally or professionally responsible for preventing irregularities (which include fraud, other illegal acts and errors). ISPPF Standard 1210. A2 states that "Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization, ***but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.***"

The responsibility for prevention of irregularities rests with Council and management through the implementation and continued operation of an adequate internal control system. Internal Auditors are only responsible for examining and evaluating the adequacy and the effectiveness of actions taken by management to fulfil this obligation.

7.4. RISK MANAGEMENT RESPONSIBILITY

Risk management is a key responsibility of the Accounting Officer and management. Internal audit is only responsible for providing assurance to management and the Audit Committee on the adequacy and effectiveness of the risk management processes. For the municipality to achieve its objectives, management should ensure that sound risk management processes are in place and functioning as intended. Internal audit shall assist both management and the Audit Committee by examining, evaluating, reporting, and recommending improvements on the adequacy and effectiveness of the risk management processes.

8. AUTHORITY

The CAE and the Internal Audit staff are authorized amongst others to:

- Have unrestricted access to all functions, records, property, and personnel.
- Have full and free access to the Audit Committee and Municipal Manager.
- Select subjects, determine scope of work, and apply the techniques required to accomplish audit objectives.
- Obtain the necessary assistance of personnel in units of the organization where they perform audits, as well as other specialized services from within or outside the organization.

The CAE and the Internal Audit staff are **not** authorized to:

- Perform any operational duties (other than audit-related) for the municipality or its affiliates.
- Initiate or approve accounting transactions external to the internal audit function.
- Direct the activities of any organization's employee not employed by the internal auditing department, except to the extent such employees have been appropriately assigned to audit teams or otherwise assist internal audit.

9. REPORTING

After completion of the audit assignments, the Internal Audit Unit shall report to management in writing any significant weaknesses observed on the internal control structure and other areas that come to its attention, which internal audit considers necessary to be brought to management's attention.

As part of Internal Audit normal audit procedures, Internal Audit shall request management to provide written comments and corrective action plans on the reported control deficiencies. The Internal Audit report together with management comments, action plans and implementation dates shall be submitted to Municipal Manager to secure action. The

executive summary together with management action plans shall also be submitted to the Audit Committee for information on a quarterly basis.

A follow-up audit shall be scheduled after the final implementation date in order to express an opinion on the corrective action taken by management to address the previously reported findings or deficiencies on internal controls.

10. ASSURANCE SERVICES, CONSULTING SERVICES AND OTHER SERVICES

10.1. ASSURANCE ENGAGEMENTS/SERVICES

ISPPF defines an assurance service as an objective examination of evidence for the purposes of providing an independent assessment on governance, risk management, and control processes for the organization. The following is an example of the nature of assurance engagements to be provided by Internal Audit, but not limited to:

- (a) Financial Audits
- (b) Compliance and Limited Regularity Audit
- (c) Performance Audit and Audit of Performance Information
- (d) IT Audit
- (e) Governance Audit

Business systems, processes, operations, functions and activities within the organisation shall be subjected to internal audit's evaluation.

10.2. CONSULTING ENGAGEMENTS/SERVICES

ISPPF defines consulting services as any advisory and related engagements, the nature and scope of which should be agreed upon with the auditee (management), which are intended to add value and improve an organization's governance, risk management, and control processes without the internal audit assuming management responsibility.

The following are examples of the nature of consulting services to be provided by Internal Audit:

- Advice
- Facilitation
- Training

And they shall be formal i.e. planned and subject to written agreement; or informal i.e. routine activities such as participating on standing committees, ad hoc meetings and routine information exchange.

However, the Internal Audit Activity shall carry out consulting and assurance services provided that their independence and objectivity may not be impaired. In cases where assurance services are provided within one year after formal consulting engagement, steps shall be taken to minimize the effect of impairment by assigning different auditor(s)

to perform each of the services, establishing independent management and supervision, defining separate accountability for the result of the projects, and disclosing the presumed impairment.

10.3. OTHER SERVICES AND AD-HOC AUDITS

All management requests for ad-hoc audits to be performed by Internal Audit shall be formally documented and be properly assessed prior being accepted. Audit committee shall approve all management requests for audits subsequent to exhaustion of normal budgeted hours for ad-hoc audit requests and such ad-hoc request shall also be forwarded to the Risk Management Unit for documentation as emerging risks. No ad-hoc requests from the political office-bearers shall be accepted by the Internal Audit.


11. STANDARDS OF PRACTICE AND CODE OF ETHICS

Internal Audit is required to perform its work in a professional manner. The Institute of Internal Auditors has established a Code of Ethics, which covers basic principles of the Internal Audit practice. THLM's Internal Audit shall therefore, observe and comply with the International Standards for the Professional Practice of Internal Auditing (SPPIA) of the Institute of Internal Auditors and abide by the Code of Ethics.

12. REVIEW AND APPROVAL

This charter shall be reviewed on an annual basis and submitted to the Audit Committee for approval.

Prepared by:


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Mrs. PB Mosomane
Chief Internal Auditor

11 / 06 / 2014
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Date

Accepted by:


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Mr. JI Sindane
Municipal Manager

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Date

Approved by:



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Mr. MA Mashego
Chairperson: Audit Committee

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Date