



**MFMA**

**MUNICIPAL AUDIT  
COMMITTEE TOOLKIT**

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REPUBLIC OF SOUTH AFRICA



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## **MUNICIPAL AUDIT COMMITTEE TOOLKIT**

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# 1. FOREWORD

The aim of this Guide and Tool pack is to provide guidance on the operation of the Audit Committees of municipalities and municipal entities operating under *the Municipal Finance Management Act, Act 53 of 2003*.

The Guide discusses a range of functions and responsibilities that are appropriate for an Audit Committee. Within this broad set of responsibilities, it is important that each committee, in consultation with the Municipal Manager/Chief Executive Officer, decide those aspects that the committee will give priority to and particularly focus on.

The Guide is intended as a reference document for Councils/Boards, Municipal Managers, Chief Executive Officers, members of Audit Committees and senior managers with responsibility for Audit Committee activities.

**This guide should be read and used together with the Municipal Public Accounts Committees (MPAC) Guide and Toolkit.**

These guidelines should be used as a tool for induction of the Audit Committee to streamline their activities in pursuit of good and quality performance in discharging their responsibilities. The guidelines should also be utilized to raise awareness to Council/Board and management of municipalities and municipal entities to fully appreciate the role of the Audit Committee.

## **2. AUDIT COMMITTEE MANUAL / GUIDE**



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### **STRENGTHENING GOVERNANCE WITHIN AUDIT COMMITTEES**

To build capacity of Audit Committees and Municipality officials on the effectiveness of Audit Committees

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## **FOREWORD**

The National Treasury (NT) of South Africa is a national government department under the executive authority of the Ministry of Finance and is responsible for coordinating macroeconomic policy and promoting the national fiscal policy framework. Its role is defined by the Constitution of the Republic of South Africa, 1996 (The Constitution) and the Public Finance Management Act, 1999 (PFMA), which regulates financial management in the public sector at national and provincial government levels. The NT coordinates intergovernmental financial relations, manages the budget preparation process and exercises control over the implementation of the annual national budget, including any adjustments budgets. The NT also performs functions assigned to it in other legislation, such as Municipal Finance Management Act 56 of 2003 (MFMA).

The NT has a constitutional and national legislative mandate to manage public sector financial matters in South Africa, including the capacity development of cash flow managers. The NT fulfils a pivotal role in the implementation and management of the PFMA and the MFMA, among others. The essence of both these Acts is to regulate financial management in the public sector at national, provincial and municipal levels respectively. The PFMA as well as the MFMA are intended to ensure that all revenue, assets, liabilities and expenditures are managed effectively and efficiently and that the responsible officials are equipped with appropriate and necessary knowledge to adhere in a compliant manner to the intentions stipulated in the respective Acts. MFMA section 34(1) states that “national and provincial governments must by agreement assist municipalities in building the capacity of municipalities for efficient and transparent financial management”. Given the complexity and scope of the capacity development challenge, implementation of any capacity development initiative will require collaborative partnerships between public and private sector stakeholders, and the international donor community.

Despite the provisions in the MFMA and the reforms developed over the last 15 years to support the implementation, enforcement still appears to be a challenge across all municipalities and municipal entities. The recently published consolidated general report on local government audit outcomes for the 2020/2021 financial year also highlighted a number of issues that led to non-compliance with the MFMA. Furthermore, it was also noted that compliance with legislation has regressed over the years with the highest percentage of non-compliance persisting.

The common areas of non-compliance relate to the following disciplines, SCM, Asset Management, Revenue Management, Liability Management, Annual Financial Statements and Annual Reports amongst others.

## **MUNICIPAL AUDIT COMMITTEE MANUAL / GUIDE - 2023**

The constitutional mandate states that the council of municipalities must strive to achieve the objectives set out in the Constitution. In executing its functions and fulfilling its obligations, Council is assisted by various functions within the governance structure of the Municipality or Municipal Entity. One such function is the **Audit Committee**. The requirements of the legislation make the composition of Audit Committees an essential consideration. Members need to have sufficient knowledge, skills and experience in a number of fields. The difficulty in attracting a pool of suitable people to serve on the municipal Audit Committees is a challenge. Municipalities do not always have sufficient budgets to compete with private sector companies in remunerating Audit Committee members. Audit Committee members are appointed with skills and experience in their respective professions and very limited experience on Audit Committee operations. This creates a need to induct Audit Committee Members prior to them assuming their responsibilities. The induction should be detailed to enable them to execute their responsibilities effectively.

These guidelines should be used as a tool for induction of the Audit Committee to streamline their activities in pursuit of good and quality performance in discharging their responsibilities. The guidelines should also be utilized to raise awareness to Council/Board and management of municipalities and municipal entities to fully appreciate the role of the Audit Committee. An effective audit committee can assist management in discharging its accountability responsibilities to safeguard assets, operate adequate systems and controls, and prepare annual financial statements, by:

- improving communication and increasing contact, understanding and confidence between management and internal and external auditors (which may result in a more cost-effective external audit, to benefit both the organisation and the auditors);
- undertaking investigations and ensuring objectivity to such reports and recommendations;
- scrutinizing the performance of internal and external auditors, thus increasing accountability;
- facilitating the imposition of discipline and control, thus reducing the opportunity for fraud;
- assisting in strengthening governance arrangement in municipalities and municipal entities;
- strengthening the objectivity and credibility of financial reporting.

The aim of the Guide is to provide guidance on the operation of the Audit Committees of municipalities and municipal entities operating under *the Municipal Finance Management Act, Act 53 of 2003*.



## **MUNICIPAL AUDIT COMMITTEE MANUAL / GUIDE - 2023**

The Guide discusses a range of functions and responsibilities that are appropriate for an Audit Committee. Within this broad set of responsibilities, it is important that each committee, in consultation with the Municipal Manager/Chief Executive Officer, decide those aspects that the committee will give priority to and particularly focus on.

The Guide is intended as a reference document for Councils/Boards, Municipal Managers, Chief Executive Officers, members of Audit Committees and senior managers with responsibility for Audit Committee activities.

Application of the guidance provided in this document will result in the Audit Committee not merely being a ceremonial function but adding value to the Municipality/Municipal Entity and the Council/Board through providing oversight and objective advice in the financial reporting process, the audit process, the system of internal controls and compliance with laws and regulations.

The Local Government: Municipal Structures Act, 1998, was amended during May 2021 to accommodate changes and enhancements to the local government environment. The Municipal Structures Amendment Act, Act 3 of 2021, Section 79A now reads:

- (1) *A municipal council must establish a committee called the municipal public accounts committee.*
- (2) *The mayor or executive mayor, deputy mayor or executive deputy mayor, any member of the executive committee, any member of the mayoral committee, speaker, whip and municipal officials are not allowed to be members of the municipal public accounts committee.*
- (3) *The municipal council must determine the functions of the municipal public accounts committee, which must include the following:*
  - (a) *review the Auditor-General's reports and comments of the management committee and the audit committee and make recommendations to the municipal council;*
  - (b) *review internal audit reports together with comments from the management committee and the audit committee and make recommendations to the municipal council;*
  - (c) *initiate and develop the oversight report on annual reports contemplated in section 129 of the Local Government: Municipal Finance Management Act;*
  - (d) *attend to and make recommendations to the municipal council on any matter referred to it by the municipal council, executive committee, a committee of the council, a member of this committee, a councillor and the municipal manager; and*
  - (e) *on its own initiative, subject to the direction of the municipal council, investigate and report to the municipal council on any matter affecting*

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*the municipality.*

- (4) *Reports of the municipal public accounts committee must be submitted to the speaker who must table such reports in the next meeting of the municipal council.*
- (5) (a) *For the purposes of this section 'audit committee' means the audit committee envisaged in section 166 of the Local Government Municipal: Finance Management Act.*  
(b) *Each municipality and each municipal entity must establish an audit committee in accordance with that section."*

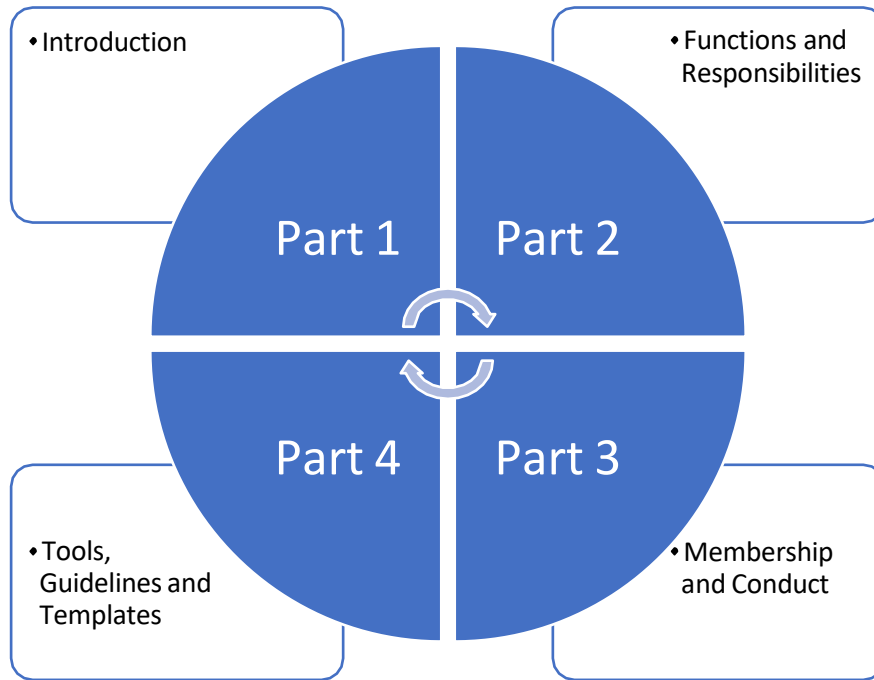
This guide should therefore be read and used together with the Municipal Public Accounts Committees (MPAC) Guide and Toolkit, the relevant National Treasury in consultation with the relevant Provincial Treasury will provide further regulations, circulars, guides, supporting measures and respond to all matters relating to Audit Committees and Internal Audit functions, roles and responsibilities to ensure uniform national norms and standards are maintained and adhered to. Internal Audit and Audit Committees to register and utilise the National Treasury's Audit Action Plan web enabled system to monitor progress in-year. In addition audit committees must provide comments to management on MFMA Section 71 and 72 reports to ensure alignment and consistency with performance indicators.

## **ATTRIBUTES AND PRACTICES OF THE EFFECTIVE AUDIT COMMITTEE**

An effective Audit Committee is distinguished by the following attributes:

- Has a clearly documented charter that:
  - has been determined having regard to relevant legislative requirements and the entity's broader corporate governance framework;
  - includes the committee's responsibilities;
  - and is approved by its Council or Board in the case of municipal entities.
- Possesses broad financial management and public sector experience and expertise.
- Has a sound working relationship with its Council/Board.
- Can exercise discretion in determining how best to meet its responsibilities.
- Adopts an independent perspective and appreciates the separation of management and Audit Committee responsibilities.
- Is knowledgeable about the Municipality's/Municipal Entity's operations, particularly its risks and the arrangements in place to management of these risks.
- Is chaired by a person who is able to lead discussions, encourage the participation of other members, and conduct meetings in an effective manner.
- Encourages and maintains an open and constructive dialogue with senior management, internal and external audit, and other committees.
- Effectively plans its activities to meet its responsibilities; focuses on the important issues and risks; is forward-looking; and adopts a continuous improvement approach in its interaction with the Municipality's/Municipal Entity's management.
- Monitors the implementation of recommendations made by internal and external audit and other review activities.
- Ensures internal audit coverage/plan:
  - is aligned with the Municipality's/Municipal Entity's risks;
  - is an appropriate mix of performance and compliance audits;
  - includes a focus on the areas of greatest risk; and
  - Ensure that quality of work of internal audit is upheld at all times.
- Receives an appropriate level of support and facilitates sufficient opportunities to keep committee members abreast of key developments in the Municipality and/or Municipal Entity.

**Structure of the guide:**



*Figure 1: Structure of the guide*

**IMPORTANT NOTE:**

The user of this guide is encouraged to read the entire guide before attempting to implement any or all of the templates, guides or checklists. This will provide for a thorough understanding of the principles and context of the municipal Audit Committee's role and responsibilities and the application of the tools to the specific size and unique complexity of the relevant Municipality/Municipal Entity.

## **PART 1**

### **1. INTRODUCTION**

Public sector, and specifically municipal Audit Committees are responsible for governance oversight at the Municipality/Municipal Entity that they serve within local government. This includes responsibilities enable through the MFMA and its regulations, to oversee all assurance providers in terms of the Combined Assurance Framework and model ensuring that it is optimally implemented. This guide will provide the reader with the necessary understanding, guidance, templates and resources to assist in the establishment and maintenance of an effective municipal Audit Committee and the attraction and retention of skilled and knowledgeable Audit Committee members.

#### **1.1 Application of the Guide**

The principles and practices outlined in this Guide are applicable to all Municipalities and Municipal Entities, irrespective of the particular governance model adopted by each Municipality/Municipal Entity.

#### **1.2 Structure of the Guide**

Part 1 of the Guide introduces the reader to the guide and the necessity for the effective functioning of Audit Committees at local government level.

Part 2 explains the detailed functions and responsibilities of municipal Audit Committees as indicated in the MFMA as well as good corporate governance principles.

Part 3 elaborates on the composition of the municipal Audit Committee in terms of chairmanship, membership and relationships with all its stakeholders. It also provides guidance on the general conduct of the municipal Audit Committee and its members and provides criteria for the measuring of the performance of the municipal Audit Committee.

Part 4 of this guide consists of a comprehensive set of tools to assist the municipal Audit Committee and its members to fulfill its constitutional, legislative and oversight role. The tools consist of templates, checklists and guiding documents which have reference to the applicable legislation they aim to comply with.

In applying the guidance set out in this document and using the tools provided there is a great expectation that the relevant municipal Audit Committee will be better equipped to fulfill its mandate and add value to the broader objectives of the Municipality or municipal entity it serves.

### 1.3 Acknowledgements

The National Treasury would like to express its appreciation to the pilot municipalities, municipal entities, their staff and individual Audit Committee members, the reference group consisting of National and Provincial Treasury officials, the European Union Commission for the support in developing the Guide.

**PART 2**

**2. THE AUDIT COMMITTEE'S FUNCTIONS AND RESPONSIBILITIES**

The Municipal Finance Management Act No 56 of 2003 (MFMA), Section 166, states as follows:

- 166**(1) *Each Municipality and each municipal entity must have an Audit Committee. subject to subsection (6).*
- (2) *An Audit Committee is an independent advisory body which must—*
- (a) *advise the municipal council, the political office-bearers. the accounting officer and the management staff of the Municipality, or the board of directors. the accounting officer and the management staff of the municipal entity. on matters relating to-*
- (i) internal financial control and internal audits;*
  - (ii) risk management;*
  - (iii) accounting policies;*
  - (iv) the adequacy, reliability and accuracy of financial reporting and information;*
  - (v) performance management;*
  - (vi) effective governance;*
  - (vii) compliance with this Act, the annual Division of Revenue Act and any other applicable legislation;*
  - (viii) performance evaluation; and*
  - (ix) any other issues referred to it by the Municipality or municipal entity;*
- (b) *review the annual financial statements to provide the council of the Municipality or, in the case of a municipal entity. the council of the parent Municipality and the board of directors of the entity, with an authoritative and credible view of the financial position of the Municipality or municipal entity. its efficiency and effectiveness and its overall level of compliance*

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*with this Act, the annual Division of Revenue Act and any other applicable legislation:*

- (c) respond to the council on any issues raised by the Auditor-General in the audit report;*
- (d) carry out such investigations into the financial affairs of the Municipality or municipal entity as the council of the Municipality, or in the case of a municipal entity, the council of the parent Municipality or the board of directors of the entity, may request: and*
- (e) perform such other functions as may be prescribed.*

In total, these represent a broad set of functions and responsibilities. It is therefore important that each committee, in consultation with its Council or Board, decide those aspects of a Municipality's/Municipal Entity's operations that the committee will give priority to and particularly focus on, whilst complying with the requirements of the MFMA.

This includes reviewing of preventative controls and advise on pro-active measures that the internal audit and audit committees recommend to management to improve outcomes in the quest to attain value for money. In addition, the value added by internal audit and audit committees can improve management's and operational efficiencies, which is an important objective.

This guide will now deal with each of the responsibilities in detail. Specific reference to the area of the MFMA is made in a block such as indicated below:

<b>Legislation</b>	<i>Reference to the MFMA or relevant legislation.</i>
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### 2.1 Internal Control

<b>Legislation</b>	<p>(2) An Audit Committee is an independent advisory body which must—</p> <p>(a) advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to-</p> <p>(i) internal financial control and internal audits</p>
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The Audit Committee will generally be responsible for reviewing the adequacy of the Municipality's/Municipal Entity's **internal control environment** in general, to provide assurance that the Municipality's/Municipal Entity's key controls are designed appropriately and are operating as intended. In fulfilling this responsibility, the committee could be expected to obtain information from management and also from internal and external audits on the design and operation of key **internal controls, including financial controls**, and assurance processes. To do this effectively, Audit Committees are expected to, and mechanisms in place to periodically assess compliance with the Municipality's/Municipal Entity's financial management responsibilities.

#### **Audit Committee internal control responsibilities**

An Audit Committee's responsibilities in relation to a Municipality's/Municipal Entity's internal controls would generally be to:

- oversee whether management's approach to maintaining an effective internal control framework, including over external parties such as contractors, is sound and effective;
- obtain assurance whether management has in place relevant policies and procedures, and that these are periodically reviewed and updated;
- determine whether appropriate processes are in place to periodically assess compliance with legislation and key policies;
- obtain assurance whether appropriate policies and supporting procedures are in place for the management and exercise of compliance, internal policy, and delegations' requirements;
- consider how management identifies any required changes to the design or implementation of key internal controls; and
- assess whether management has taken steps to embed a culture which is committed to ethical and lawful behaviour.

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**2.2 Internal Audit**

<b>Legislation</b>	<p>(2) <i>An Audit Committee is an independent advisory body which must—</i></p> <p style="padding-left: 20px;"><i>(a) advise the municipal council, the political office-bearers. the accounting officer and the management staff of the Municipality, or the board of directors.the accounting officer and the management staff of the municipal entity. on matters relating to-</i></p> <p style="padding-left: 20px;"><i>(i) internal financial control and internal audits;</i></p>
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According to the Institute of Internal Auditors definition of internal auditing: “*Internal audit is an independent, objective assurance and consulting activity designed to add value and improve an entity’s operations. It helps an entity accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.*”

A strong relationship between the Audit Committee and the Municipality’s/Municipal Entity’s internal auditors enables the Audit Committee to meet its responsibilities and carry out its functions. Internal Audit is a major source of information and assurance to the Audit Committee on the performance of the Municipality or Municipal Entity and its control environment. To maximize the value provided by Internal Audit to the Audit Committee, it is important that open lines of communication are established and maintained between Internal Audit and the Audit Committee. This communication line is referred to as the Functional Reporting line of Internal Audit.

**Audit Committee Internal Audit responsibilities**

The Audit Committee has oversight responsibilities over the effective functioning of Internal Audit within a Municipality and Municipal Entity. This oversight responsibility covers the planning, execution and reporting of Internal Audit against the approved Internal Audit plan and Charter which are approved by the Audit Committee. The Chief Audit Executive (CAE) must ideally report internally within the Municipality/Municipal Entity to the Accounting Officer (Municipal Manager/Chief Executive Officer). This is referred to as the Administrative Reporting line of Internal Audit. Reporting to the most senior officer in the Municipality/Municipal Entity has a positive effect on the independence of the Internal Audit function.

Organizational independence is effectively achieved when the chief audit executive reports functionally to the audit committee. Examples of functional reporting to the Audit Committee, which enhances the independence and objectivity of Internal Audit, involves, but is not limited to, the following:

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- Approval of the Internal Audit Charter, for acceptance by the Accounting Officer/Municipal Manager;
- Approval of the risk-based Internal Audit plan;
- Concurring with and providing input on the Internal Audit budget allocation and resource plan for approval by the Accounting Officer/Municipal Manager;
- Receiving communications from the CAE on the internal audit activity's performance relative to its plan and other matters;
- Concurring with and providing input regarding decisions during the appointment, removal of the CAE, and performance assessments of the Internal Audit function;
- Making appropriate inquiries of management and the CAE to determine whether there is inappropriate scope or resource limitations.

The Audit Committee should understand the environment within which the Internal Audit function operates. Audit Committee members should also understand what the MFMA and its regulations, Institute of Internal Auditors (IIA) requires of the Internal Audit function. Even if an independent quality review (refer to Part 3 section 4.5 for detail) is done on an Internal Audit function and the results of the review are reported to the Audit Committee, the Audit Committee members should have sufficient knowledge to create and support an environment that enhances efficiency and compliance of the Internal Audit function, where functionality is concerned. As a minimum, the Audit Committee should oversee the following with regards to the Internal Audit function:

- 2.2.1 Review and approve the Internal Audit charter annually or amend if there are any changes in legislation or the Municipality's/Municipal Entity's operating environment. As a minimum, the Internal Audit charter should include:
- a. The mission, purpose and authority of the Internal Audit function
  - b. Its status and its place in the Municipality's/Municipal Entity's structure
  - c. Responsibilities of the Internal Audit function
  - d. Relationship with management, other assurance providers and external audit (combined assurance)
  - e. Operational issues such as assurance and consulting activities
  - f. Assessment of the Internal Audit function's performance

An example of a typical Internal Audit Charter is provided under section 3 Guiding Documents with reference PSAUC7.

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- 2.2.2 Oversees that the Internal Audit function adheres to and conforms with the International Professional Practices Framework (IPPF) of the Institute of Internal Auditors. The information on conformance with the IPPF will originate from the Quality Assurance and Improvement Program (QAIP) of the Internal Audit function. (Refer to Part 3 section 4.5 for detail on the QAIP).
- 2.2.3 Regularly review the functional and administrative reporting lines of internal audit to ensure that the organizational structure is consistent with the principles of independence and accountability.
- 2.2.4 Review the annual independence declaration of internal audit.
- 2.2.5 Where the Chief Audit Executive is expected to have roles and/or responsibilities that fall outside of internal auditing, ensure that the necessary safeguards are implemented and maintained to limit the potential impairments to independence and objectivity. Examples of roles outside of the normal responsibilities of the CAE could include responsibility for Risk Management, Combined Assurance, Compliance Management, etc. Managing the independence of the Internal Audit function in these cases could involve the consideration of outsourcing of the assurance function for these activities.
- 2.2.6 Ensure the Internal Audit function at least reports annually on its Quality Assurance and Improvement Programme (QAIP).
- 2.2.7 Ensure that the Internal Audit function (whether in-house, co-sourced and/or outsourced) is subjected to an external independent quality review in line with IIA Standards and as when the Audit Committee determines it appropriate, but at least within 5 years of the previous review, as a measure to ensure the function remains effective.
- 2.2.8 The Audit Committee should assess the options for sourcing Internal Audit and consider, amongst others, issues such as size of the Internal Audit Function, complexity of the operations, available budget, and the ability of the Audit Committee to execute its duties suitably. Sourcing options could include:
- a) In-house function where all Internal Audit staff members are employed by the municipality/municipal entity and the Internal Audit methodology is dictated by the in-house Chief Audit Executive;
  - b) Co-sourced function where the in-house capacity and skills of the Internal Audit activity are enhanced by staff members from an outside consulting firm with whom we contract. The Internal Audit methodology of the in-house Chief Audit Executive is still followed, and the CAE remains responsible for the overall quality of work delivered; or
  - c) Full outsourced Internal Audit activity where the Chief Audit Executive and all Internal Audit staff members are provided by an external consulting firm

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and the municipality/municipal entity typically adopts the Internal Audit methodology of the consulting firm.

- 2.2.9 Assess adequacy of skills and size of Internal Audit staffing versus complexity of the Municipality/Municipal Entity and changes in the operating environment. Reviewing and providing input on the organogram for Internal Audit.
- 2.2.10 Review a 3-year training program for the Internal Audit function to ensure that there is appropriate attention given to quality, report writing skills and keeping abreast of developments and changes in the field of Internal Audit and that staff are maintaining their ongoing professional development.
- 2.2.11 Ensure that there is a transfer of skills by contractors to Internal Audit staff as appropriate.
- 2.2.12 Assist in the recruitment process and performance appraisal of the CAE as well as, retention or dismissal of the CAE which then reinforces the clear reporting line to the Audit Committee as opposed to management.
- 2.2.13 Approve the risk-based Internal Audit plan through reviewing and assessing the coverage and adequacy of the Internal Audit plan when compared with the risks facing the Municipality/Municipal Entity and the effect of the combined level of assurance on the risks and the results of the external audit. As a minimum the risk-based internal audit plan should cover:
  - a. Operational effectiveness and efficiencies across processes
  - b. Financial reporting – prevention and detection of accounting errors, control weaknesses and fraud
  - c. Compliance with laws, regulations and internal policies
  - d. Information technology (IT) – systems and internal functioning of the IT department
  - e. Effectiveness of risk management within the Municipality/Municipal Entity
  - f. Assessment of strategy, business plans and budgets
  - g. Performance setting, monitoring and reporting

The approval of the Internal Audit plan should be scheduled as soon as possible in the new financial year to give the Internal Audit activity enough time to complete the plan during the year.

- 2.2.14 Consider the Internal Audit Strategy to determine appropriate attention to stakeholder expectations and alignment with the strategy of the Municipality/Municipal Entity.

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- 2.2.15 Review and provide input on the allocation of the budget of Internal Audit in line with the annual internal audit plan and the alignment of hours on the Internal Audit plan versus the budget being presented.
- 2.2.16 Encourage cooperation between External and Internal Audit. Review coverage and scope between External and Internal Audit to avoid duplication and possible cost savings from the alignment of the two functions. Timing of internal audits and the months during the financial period that the audit scope will cover must be aligned. In some cases, reports from Internal Audit cannot be used by the external auditors due to focus areas of relevant risks.
- 2.2.17 Review and track quarterly progress of Internal Audit against the approved Internal Audit plan for the year and ensuring that reports are tabled timeously after completion. Targets should be set in the CAE performance contract on the achievement of the plan and the timeous submission of reports to the Audit Committee.
- 2.2.18 Review and approve reports from Internal Audit on a quarterly basis in line with the Internal Audit plan. When the Audit Committee reviews such reports attention should be paid to issues/findings and the impact on the overall risks facing the Municipality/Municipal Entity and any impact on the financial year- end external audit. It can be one of the early warning indicators to management and the Audit Committee.
- 2.2.19 Ensure open lines of communication between the Audit Committee and the Internal Audit function. This can be implemented by having an agenda point added for an in-camera session which can be scheduled at each of the quarterly Audit Committee meetings where Internal Audit meets separately with the Audit Committee and discusses issues.
- 2.2.20 Monitor and evaluate the effectiveness and quality assurance of the Internal Audit function. This can be performed by having an independent review being performed every 5 years with an implementation plan being drafted to address the issues/findings. Performance targets must be set for the CAE in his/her annual performance contract arising from such an evaluation so that there is alignment between the need for having an effective Internal Audit function and the allocation of such accountability and responsibility.

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- 2.2.21 Review policies affecting the functioning of Internal Audit such as the Internal Audit charter in the Municipality/Municipal Entity as well as understanding the methodology for sampling techniques, audit tests, the use of computer assisted audit techniques to improve on coverage of populations being tested. Policies should create a flexible and dynamic environment that is able to address emerging business and operational assurance needs.
- 2.2.22 Understand the format of reports being presented by Internal Audit, the rating scales used to assess, rate and finally conclude on the overall functioning of the area being audited as well as the alignment and link in with the impact on the operational and strategic risk register. It is suggested that as part of the orientation for new members of the Audit Committee that Internal Audit should be able to disseminate their reports and workshop them so that members have a clear understanding of how a report is compiled and what information is being presented as this will aid in the members ability to make decisions from their review of reports being presented during their tenure.
- 2.2.23 Recommend the appointment of an external service provider if the Internal Audit function is outsourced. This would typically occur every 3 to 5 years and the sourcing of tenders should be started at least 12 months prior to the planned rotation.
- 2.2.24 Review of any reports from Internal Audit on limitation of scope, extension of audit deadlines beyond 3 months by management, repeated cancellation of scheduled audits unnecessarily and decide on the way forward.
- 2.2.25 Preside over disagreements between management and internal auditors ensuring that open communication lines are promoted at all times. A formal process should be documented and circulated as part of the service level agreement from Internal Audit that covers how disagreements will be dealt with and the escalation processes to be followed.
- 2.2.26 Strive towards setting a tone where an Internal Audit function has the confidence and courage to report any significant issues even if it involves executive management. The Audit Committee must also protect Internal Audit functions who report such information from the possible falling out with the entities' executive management team. Such reports can also be submitted to National and Provincial Treasuries to assist in performing their oversight functions in terms of the MFMA.
- 2.2.27 Review and assess the written assessment prepared by Internal Audit regarding internal financial controls.

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**2.3. Risk management**

<b>Legislation</b>	<p><i>(2) An Audit Committee is an independent advisory body which must—</i></p> <p><i>(a) advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to-</i></p> <p><i>(ii) risk management</i></p>
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Risk management is the culture, processes and structures that are directed towards realizing potential opportunities while managing adverse effects. Risk management is an essential part of effective corporate governance.

Municipalities and municipal entities are bound by their Constitutional mandates to provide services or products in an efficient, cost effective and economical way. No Municipality/Municipal Entity functions in a risk-free environment and in fulfilling their mandates Municipalities/Municipal Entities are especially vulnerable to risks while being ripe for opportunities at the same time. Many of the functions within the scope of the local government mandate pose substantial risk exposures but which cannot be avoided in the interest of the public good. Local government institutions therefore characterise elevated risk profiles. This places an extra duty of care on decision makers and managers to ensure that risks are properly managed and the Institution is able to fulfil its mandate notwithstanding the inherent riskiness. Risk management is a valuable management tool which increases a Municipality's/Municipal Entity's prospects of success through minimizing negative outcomes and optimizing opportunities.

Local and international trends confirm that risk management is a strategic imperative rather than an option within high performing institutions. A hallmark of high performing institutions is that they set clear and realistic strategies, develop achievable objectives aligned to the strategies, understand the intrinsic risks associated therewith and direct resources towards managing such risks based on cost-benefit principles.

The Audit Committee is the only committee recognized in the MFMA as being responsible for the oversight of risk management.



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Although ultimate accountability for the management of risk remains with the Municipal Manager/Chief Executive Officer, the Municipal Manager/Chief Executive Officer will generally, seek assurance from the Audit Committee that management has in place policies and arrangements designed to demonstrate that the operation of a Municipality's/Municipal Entity's risk management arrangements are appropriate and operationally effective. This assurance role can extend to assisting the overall alignment and integration of risk management plans and the integration of risk management into business planning and program implementation activities. Effective Audit Committees will also generally have a key role in providing assurance that management has in place effective risk management practices when implementing high risk projects, programs and/or activities.

### **Audit Committee Risk Management Responsibilities**

The responsibilities of the Audit Committee with respect to risk management should be formally defined in its Charter.

An Audit Committee's responsibilities in relation to risk management would generally be to:

- oversees whether management has in place a current and comprehensive enterprise risk management framework and associated procedures designed to ensure that the identification and management of the Municipality's/Municipal Entity's business and financial risks, including fraud, are effective;
- determine whether a sound and effective approach has been followed in managing the Municipality's/Municipal Entity's major risks including those associated with individual projects, program implementation, and activities;
- assess the impact of the Municipality's/Municipal Entity's enterprise risk management framework on its control environment and insurance arrangements;
- determine whether a sound and effective approach has been followed in establishing the Municipality's/Municipal Entity's business continuity planning arrangements, including whether business continuity and disaster recovery plans have been periodically updated and tested;
- review the Municipality's//Municipal Entity's fraud control arrangements and satisfy itself the Municipality/Municipal Entity has appropriate processes or systems in place to capture and effectively investigate fraud-related information; and

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- review reports on fraud from the Municipality's/Municipal Entity's Fraud Manager that outline any identified allegations of fraud, the status of any ongoing investigations and any changes to identified fraud risk in the Municipality/Municipal Entity.

Where there is no separate Risk Committee, the risk oversight responsibilities of the Audit Committee should be identical to those ascribed to the Risk Committee by the National Treasury Framework, namely to:

- (i) review and recommend for the Approval of the Municipal Manager/Chief Executive Officer, the:
  - (ii) risk management policy;
  - (iii) risk management strategy;
  - (iv) risk management implementation plan;
  - (v) Institution's risk appetite, ensuring that limits are:
    - supported by a rigorous analysis and expert judgement;
    - expressed in the same values as the key performance indicators to which they apply;
    - set for all material risks individually, as well as in aggregate for particular categorizations of risk; and
    - consistent with the materiality and significance framework.
  - (vi) Institution's risk tolerance, ensuring that limits are supported by a rigorous analysis and expert judgement of:
    - the Institution's ability to withstand significant shocks; and
    - the Institution's ability to recover financially and operationally from significant shocks.
- (i) Institution's risk identification and assessment methodologies, after satisfying itself of their effectiveness in timeously and accurately identifying and assessing the Institution's risks.
  - b) evaluate the extent and effectiveness of integration of risk management within the Institution;
  - c) assess implementation of the risk management policy and strategy (including plan);
  - d) evaluate the effectiveness of the mitigating strategies implemented to address the material risks of the Institution;

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- e) review the material findings and recommendations by assurance providers on the system of risk management and monitor the implementation of such recommendations;
- f) develop its own key performance indicators for approval by the Municipal Manager/Chief Executive Officer; and
- g) provide timely and useful reports to the Municipal Manager/Chief Executive Officer on the state of risk management, together with accompanying recommendations to address any deficiencies identified by the Committee.

Responsibilities of the Audit Committee, where there is a separate Risk Management Committee, should include:

- reviewing and recommending disclosures on matters of risk in the annual financial statements and annual report;
- reviewing and providing regular feedback to the Municipal Manager/Chief Executive Officer on the adequacy and effectiveness of risk management in the Municipality/Municipal Entity, including recommendations for improvement;
- ensuring that the Internal Audit and Auditor-General plans are aligned to the risk profile of the Municipality/Municipal Entity;
- providing oversight over the combined assurance process;
- reviewing and concurring with the Municipality's/Municipal Entity's risk appetite;
- receiving and considering reports from the Risk Committee;
- satisfying itself that it has appropriately addressed the following areas:
  - financial reporting risks, including the risk of fraud;
  - internal financial controls; and
  - IT risks as they relate to financial reporting.
- evaluate the effectiveness of Internal Audit in its responsibilities for risk management.

Where the Municipal Manager/Chief Executive Officer agrees that the Audit Committee will have an assurance role in relation to individual projects, programs or activities, it is important that the committee's role is formalized and included in the governance arrangements for the project, program or activity.

The determination of whether a separate Risk Committee should be formed is informed, amongst other, by the type or category of municipality as indicated by the Municipal Structures Act of 1998.

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The table below can be used as guidance in this regard, but every municipality must decide on their own structure in accordance with their unique environment, size and demands.

<b>Municipal Category</b>	<b>Explanation and Example</b>	<b>Audit Committee / Risk Committee Consideration</b>
Category A	Metropolitan Municipality <ul style="list-style-type: none"> <li>• Six biggest cities in SA</li> <li>• More than 500 000 voters</li> <li>• Metropolitan Municipality co-ordinates delivery of services to the whole area.</li> </ul>	Separate Audit Committee and Risk Committee due to size and complexity of risk environment
Category B	Local Municipality <ul style="list-style-type: none"> <li>• Broken into Wards represented by Ward Councillors</li> </ul>	Combined Audit and Risk Committee depending on size and complexity of risk environment
Category C	District Municipality <ul style="list-style-type: none"> <li>• Number of Local Municipalities within a district</li> <li>• Co-ordinate service delivery in the whole district</li> </ul>	Separate Audit Committee and Risk Committee due to size and complexity of risk environment

*Table 1: Determination of a Separate Risk Committee*

Review of a Municipality's/Municipal Entity's management of fraud risks is generally undertaken as an integral part of an Audit Committee's risk management responsibilities. An Audit Committee can play a key role in securing awareness that fraud control interacts and links with other governance frameworks across the Municipality/Municipal Entity. Fraud risk should not be looked at in isolation from the general business of the Municipality/Municipal Entity but should be considered as an aspect of the Municipality's/Municipal Entity's broader risk assessment processes, including the security risk assessment.

In order to exercise appropriate oversight and to provide meaningful counsel under this critical mandate, the Audit Committee must have detailed knowledge and understanding of the Municipality's/Municipal Entity's:

- mandate, objectives and performance targets;
- significant risk factors and opportunities;

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- system of risk management - including the process for identifying, evaluating, prioritizing and managing risks, and monitoring the effects of actions taken to manage risks within predetermined parameters;
- risk governance - including the appropriateness of the risk policy and strategies, institutional (structural) arrangements and capacity to manage risk;
- the current risk profile and actions proposed or being taken to manage risks falling outside predetermined parameters, and to exploit opportunities; and
- emerging risks, the Municipality's preparedness to cope, and plans to build resilience.

The Audit Committee needs to develop this knowledge through its own initiatives as well as through engagements with at least the following stakeholders:

- Council/Board;
- Municipal Manager/Chief Executive Officer;
- Executive management;
- Senior/Line management (heads of the various business units);
- Risk management committee (and its sub committees if necessary);
- Auditor-General of South Africa or External auditors;
- Internal auditors; and
- Other assurance providers (including regulatory authorities, monitoring and oversight authorities, etc.)

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**2.4 Financial statements**

<b>Legislation</b>	<p>(2) <i>An Audit Committee is an independent advisory body which must—</i></p> <p>(a) <i>advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to-</i></p> <p style="padding-left: 40px;">(iii) <i>accounting policies</i></p> <p style="padding-left: 40px;">(iv) <i>the adequacy, reliability and accuracy of financial reporting and information;</i></p> <p>(b) <i>review the annual financial statements to provide the council of the Municipality or, in the case of a municipal entity, the council of the parent Municipality and the board of directors of the entity, with an authoritative and credible view of the financial position of the Municipality or municipal entity, its efficiency and effectiveness and its overall level of compliance with this Act, the annual Division of Revenue Act and any other applicable legislation:</i></p>
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Section 122 of the MFMA requires that every Municipality and Municipal Entity must for each financial year prepare financial statements which fairly presents:

- the state of affairs of the Municipality or Entity;
- its performance against its budget;
- its management of revenue, expenditure, assets and liabilities;
- its business activities;
- its financial results; and
- its financial position as at the end of the financial year.

The MFMA further requires that the financial statements must be prepared in accordance with generally recognised accounting practice.

Therefore, in order for management to meet the requirements of the MFMA, the financial statements should be prepared and presented in accordance with the effective Standards of GRAP.

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The municipal manager/Chief Executive Officer as the accounting officer of the Municipality/Municipal Entity is responsible for ensuring that the financial statements fairly present the financial position, financial performance, statement of changes in net assets and cash flow information. The MFMA further requires the financial statements to be audited by the Auditor-General to ensure that the financial information is reliable, accurate, complete and a fair presentation of the effect of transactions and events in accordance with the applicable accounting standards have been achieved.

Audit Committee members, especially independent members, are not present on a daily basis, nor does the committee have sufficient time to physically review every detail of the financial statements such as agreeing whether a subsidiary ledger agrees to the financial statements.

Audit Committees should however play the following pivotal roles with regards to the Municipality's/Municipal Entity's financial statements:

- Reviewing systems, policies and processes around financial reporting and quarterly reporting;
- Requesting management to complete financial statements and performance reports for every quarterly meeting rather than receiving summarized information;
- Proactively reviewing the combined assurance processes of organizations, including proactive risk management and assurance;
- Approving internal audit plans with assurance on the internal controls over financial and performance reporting, and if need be, extending to a review against the applicable standards;
- Critically evaluating management action plans to address external audit and internal audit findings, including assessing whether the action plans will practically address the issues raised;
- Monitoring the action plan and obtaining explanations on reasons for not implementing;
- Critically reviewing the Interim and Annual Financial Statements, including disclosures to the financial statements, and performance report against the knowledge of the entities, as well as expectations of the performance based on the observations during the year;
- Proactively engaging with the AGSA and internal audit on critical reporting risks prior to the financial statements and performance reports being prepared;
- Continuously reporting to the oversight bodies including the executive authority of the reporting process and likely risks emanating from the financial and

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performance reporting processes;

- Liaise and collaborate with the Municipal Public Accounts Committee (MPAC) regarding financial statement review aspects and action plans to address past anomalies;
- Observe the planning process for developing and publishing of Interim and Annual Financial Statements.
  - Audit Committees should observe the annual guidance provided by National and Provincial Treasuries, where specific timelines and requirements are indicated.

Audit Committee members should also consider attending Generally Recognized Accounting Practices (GRAP) seminars and workshops to enhance their skills and understanding of the complexities and risks associated with financial statements.



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### 2.5. Performance Management

<b>Legislation</b>	<p>(2) <i>An Audit Committee is an independent advisory body which must—</i></p> <p>(a) <i>advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to-</i></p> <p>(v) <i>performance evaluation;</i></p>
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Part of the responsibilities of the Audit Committee include the review of the performance management. The Municipality/Municipal Entity must review its committees to ensure that in cases where there is an Audit Committee and a performance Audit Committee, that these are combined into one committee for effective management, oversight and reporting, as envisaged by section 166 of the MFMA. During the transition the Chairperson of the performance Audit Committee should report progress on a quarterly basis to the Audit Committee.

The Audit Committee members need to have a good understanding of the performance of the Municipality and its Entities. These include:

- Review and comment on compliance with statutory requirements and performance management best practices and standards;
- Review and comment on the alignment of the Integrated Development Plan, the Budget, Service Delivery and Budget Implementation Plan and performance agreements;
- Review and comment on relevance of indicators to ensure they are measurable and relate to services performed by the Municipality/Municipal Entity and its entities;
- Review compliance with in-year reporting requirements;
- Review the quarterly performance reports submitted by internal audit;
- Review and comment on Municipality's/Municipal Entity's and entities annual financial statements and timely submission to the Auditor-General by 31 August, each year;
- Review and comment on the Municipality's/Municipal Entity's and entities annual reports within the stipulated timeframes;
- Review and comment on the Municipality's/Municipal Entity's performance management system and make recommendations for its improvement; and
- Obtain assurance from the Internal Audit activity on the completeness and accuracy of performance information in support of the Audit Committee's assessment of the

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performance throughout the organization.

- In this regard reliance should be placed on the Combined Assurance process to obtain assurance from other lines of defense as well, as Internal Audit cannot provide complete assurance but only reasonable assurance.

The following table summarizes the roles and responsibilities of the Audit Committee in the performance management process.

<b>General</b>
<ul style="list-style-type: none"><li>• The Audit Committee’s roles and responsibilities in the performance management process should be clearly articulated in the approved Audit Committee charter.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee should review the auditing concerns in respect of performance management identified by internal and external audit, ensure adequate corrective actions are taken to address the findings identified and follow up on implementation of the said corrective actions.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee needs to review and comment on whether an appropriate process is in place to review compliance with legislation, guidelines and best practices relating to performance management.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee should include an Audit Committee member/s with appropriate performance management skills.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee needs to demonstrate a good understanding of the performance of the Municipality/Municipal Entity.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must review and comment on the Municipality’s/Municipal Entity’s Performance Management System (PMS) and make recommendations for improvement.</li></ul>
<b>Planning</b>
<ul style="list-style-type: none"><li>• The Audit Committee must review and comment on alignment between planning documents, budget and performance agreements.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must consider any changes to the planning documents and budgets during the year for reasonableness and the impact thereof on the alignment between the various strategic documents.</li></ul>

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<b>Setting key performance indicators and targets</b>
<ul style="list-style-type: none"><li>• The Audit Committee needs to advise the Council/Board with regards to the setting of Key Performance Indicators (KPI's) and targets.</li></ul>
<ul style="list-style-type: none"><li>• In reviewing the PMS, the Audit Committee must focus on economy, efficiency, effectiveness of KPIs and performance targets.</li></ul>
<b>Monitoring Performance</b>
<ul style="list-style-type: none"><li>• The Audit Committee must review compliance with in-year reporting requirements.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must ensure that the Municipality/Municipal Entity has established mechanisms to monitor its performance, PMS and the performance information generated by the system.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee needs to ensure that internal audit audits the results of performance measurements, including the functionality of the PMS, compliance of the PMS with the relevant legislation, consistency between planning documents and reports, and reliability of performance information.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must review the quarterly reports on performance management submitted by internal audit.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must review and comment on alignment between planning documents and in-year reports.</li></ul>
<b>Measure and Review Performance</b>
<ul style="list-style-type: none"><li>• The Audit Committee must ensure that the Municipality/Municipal Entity has established mechanisms to measure and review its performance against its objectives as well as the KPIs and targets set in the planning document.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must review the PMS and make recommendations to the Council/Board by way of an Audit Committee report twice a year.</li></ul>
<b>Improve Performance</b>
<ul style="list-style-type: none"><li>• The Audit Committee must advise and make recommendations to the Council's/Board's political office bearers, the Municipal Manager/Chief Executive Officer and the management staff on matters relating to performance management.</li></ul>

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<b>Measure and Review Performance</b>
<ul style="list-style-type: none"><li>• The Audit Committee must ensure that the Municipality/Municipal Entity has established mechanisms to measure and review its performance against its objectives as well as the KPIs and targets set in the planning document.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must review the PMS and make recommendations to the Council/Board by way of an Audit Committee report twice a year.</li></ul>
<b>Improve Performance</b>
<ul style="list-style-type: none"><li>• The Audit Committee must advise and make recommendations to the Council's/Board's political office bearers, the Municipal Manager/Chief Executive Officer and the management staff on matters relating to performance management.</li></ul>
<b>Report</b>
<ul style="list-style-type: none"><li>• The Audit Committee must review and comment on annual financial statements and the annual performance report and ensure timely submission to the Auditor-General.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must review and comment on the annual reports within the stipulated time frames.</li></ul>
<ul style="list-style-type: none"><li>• The Audit Committee must comment on in-year management reports in the annual report.</li></ul>
<ul style="list-style-type: none"><li>• The report of the Audit Committee needs to refer to the following aspects relating to performance management:<ul style="list-style-type: none"><li>○ Compliance with statutory requirements and performance management best practices and frameworks.</li><li>○ Alignment among planning documents, budget, performance agreements and in-year and annual reports.</li><li>○ Quarterly reports submitted by internal audit.</li><li>○ Annual financial statements and timely submission to the Auditor-General.</li><li>○ Annual reports (including the annual performance report) within the stipulated time frames.</li><li>○ The PMS, including recommendations for improvement.</li></ul></li></ul>

**2.6 Effective Governance**

<b>Legislation</b>	<p><i>(2) An Audit Committee is an independent advisory body which must—</i></p> <p><i>(a) advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to—</i></p> <p><i>(vi) effective governance;</i></p>
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The general definition of Corporate Governance includes all the structures, systems, processes, procedures and controls within an organization, at both oversight and monitoring level, and within the management structures of the organization, which are designed to ensure that an organization achieves its service delivery objectives. That it does so within sensible risk management parameters, and that it does so effectively, ethically and equitably.

The corporate governance responsibility of the Audit Committee is to provide reasonable assurance in respect of the following:

- Reasonable assurance that employees comply with relevant laws and regulations;
- That all municipal employees are conducting its affairs ethically; and
- That the Municipality/Municipal Entity is maintaining an effective and efficient system of internal control in order to prevent and detect conflicts of interest and prevent the possibility of fraud.

**Municipality/Municipal Entity governance arrangements**

Governance arrangements vary depending on a Municipality's/Municipal Entity's size, complexity and nature. Municipality/Municipal Entity governance arrangements can change over time due to, for example, legislative changes that may increase or decrease a Municipality's/Municipal Entity's responsibilities. Audit Committees must periodically review the effectiveness of their Municipality's/Municipal Entity's governance arrangements or elements of the arrangements as determined by the Municipal Manager/Chief Executive Officer and suggest improvements, where appropriate, to the Municipal Manager/Chief Executive Officer.

### **Performance reporting framework**

The Audit Committee must review the Municipality's/Municipal Entity's performance reporting framework. Municipalities/Municipal Entities generally measure their performance against a range of indicators, not just the Municipality's/Municipal Entity's 'bottom line.' Performance reporting frameworks or regimes should link directly with organizational objectives and outcomes.

The committee's responsibilities in relation to the Municipality's/Municipal Entity's performance must be undertaken in a similar way to its review of the Municipality's/Municipal Entity's risk management framework.

It is recognized that review of a Municipality's/Municipal Entity's performance reporting regime is a significant task for an Audit Committee, particularly where a Municipality/Municipal Entity has a range of performance measures across a number of programs. As such, the capacity of the committee and the maturity of the Municipality's/Municipal Entity's performance regime are factors that should be taken into account in determining the committee's scope and focus in this area.

### **Parliamentary committee reports and recommendations**

Another important responsibility of Audit Committees can be to monitor management's consideration of relevant parliamentary committee reports and external reviews; and where appropriate, monitor the implementation of associated recommendations. This responsibility is consistent with the committee's responsibilities in relation to internal and external audit reports and recommendations.

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**2.7 Compliance requirements**

<b>Legislation</b>	<p><i>(3) An Audit Committee is an independent advisory body which must—</i></p> <p><i>(a) advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to—</i></p> <p><i>(vii) compliance with this Act, the annual Division of Revenue Act and any other applicable legislation;</i></p>
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The Audit Committee must advise the Municipality/Municipal Entity on its compliance with relevant legislation, regulations and associated government policies.

Municipal compliance can be grouped into four broad categories:

- legislation and policy administered by the Municipality/Municipal Entity that it also needs to comply with;
- framework legislation and policy such as the MFMA and annual Division of Revenue Act and related regulations and policies;
- legislation and policy that has general application to the Municipality/Municipal Entity in areas such as security, occupational health and safety, privacy, and freedom of information; and
- international conventions where the Municipality/Municipal Entity enters into transaction with organizations in other countries.

Municipalities must comply with a considerable volume and complexity of legislation and policy. It would therefore be expected that Audit Committees will focus on those aspects that pose the highest risk to the Municipality/Municipal Entity, and on how the Municipality/Municipal Entity manages its compliance responsibilities.

An important responsibility of Audit Committees is reviewing the processes management has in place designed to ensure the Municipality/Municipal Entity is kept up to date with new legislation or changes to existing legislation relevant to the Municipality/Municipal Entity.

**Audit Committee compliance with legislative and policy requirements**

An Audit Committee's responsibilities in relation to legislative and policy compliance would generally be to:

- review the effectiveness of the system for monitoring the Municipality's/Municipal Entity's compliance with those laws, regulations and associated government policies/regulations that the Municipality/Municipal Entity administers and must comply with;
- determine whether management has appropriately considered legal and compliance risks as part of the Municipality's/Municipal Entity's enterprise risk management plan;
- provide advice to the Council/Board and Municipal Manager/Chief Executive Officer regarding the issue of the Municipality's/Municipal Entity's annual Compliance Report;
- if and when the Municipality/Municipal Entity enters into transactions with organizations from other countries; review, where relevant, the Municipality's/Municipal Entity's compliance with International Conventions, particularly the Organization for Economic and Co-operation and Development (OECD), the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, etc. and
- provide advice to the Council/Board and the Municipal Manager/Chief Executive Officer regarding the Municipality's/Municipal Entity's reporting responsibilities in relation to fraud and security.



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**2.8 Other relevant responsibilities**

Other responsibilities that Audit Committees may have are outlined below.

<b>Legislation</b>	<p><i>(4) An Audit Committee is an independent advisory body which must—</i></p> <ul style="list-style-type: none"><li><i>(a) advise the municipal council, the political office-bearers, the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to-</i></li><li><i>(xii) any other issues referred to it by the municipality or municipal entity;</i></li></ul>
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This guide deals specifically with two important other responsibilities of audit committees towards External Audit and the Combined Assurance Framework within the Municipality/Municipal Entity. This should include consideration by the audit committee of any matter referred to it by Council/Board of the Municipality or Municipal Entity.

## 2.9 External audit

Public sector Audit Committees are responsible for governance oversight at the entity that they serve within the national, provincial and local government. This involves a responsibility to oversee all assurance providers in terms of the Combined Assurance Framework and model ensuring that it is optimally implemented.

The Auditor-General South Africa (AGSA) is the supreme audit institution of South Africa and is responsible, in terms of the Constitution, to express an opinion on the financial statements, report on the performance report of public institution against their objectives and report any material non-compliance with laws and regulations according to the mandate provided by Public Audit Act, 2004 (Act N. 25 of 2004 as amended by Public Audit Act No.5 of 2018) (PAA). Most audits conducted in the public sector are performed by the AGSA.

One of the important relationships to be formed by the Audit Committee is with the external auditors. This relationship will enable the Audit Committee to gain insight into the audit process. This is a symbiotic relationship, where on one hand, input is obtained from the Audit Committee and on the other, the Audit Committee is evaluated by the auditors.

On the one hand there is the presentation of the engagement letter which sets out the details of how the audit will be conducted. In the public sector this often includes additional focus areas and responsibilities other than those normally covered in a private sector audit. Another aspect is the audit strategy which is presented to the Audit Committee prior to the commencement of the audit with the objective of obtaining insight on the assessment of significant risks ensuring that they are adequately addressed during the audit.

On the other hand, an important aspect of this relationship is the evaluation by the external auditors, of the assurance provided by the Audit Committee, amongst other assurance providers, in ensuring that internal control processes adequately address risks. This assessment is presented in the published annual audit outcomes report for the MFMA cycles.

This creates an interesting dynamic to the relationship between these two critical role players which must be carefully managed in order that neither role is negatively impacted. This can be achieved in several ways:

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### 2.9.1 Public Sector Audit Committee Forum (PSACF) guidance

- The PSACF has published “*The role of Audit Committees in relation to the external and internal audit*” process paper that provides guidance to Audit Committee members in their role, especially with added audit focus in the public sector, helping to navigate the issues that the Audit Committee faces in the external audit process.

### 2.9.2 Audit engagement performance and conclusion

- An audit strategy which contains further information on the following, will be developed:
  - Assessment of the significant risks raised by the auditors which should correspond with those observed by the Audit Committee during the period.
  - Understanding of any potential material irregularities that the AGSA has raised in the prior and current audit period. The amount of reliance on work performed by other assurance providers including use of work by the internal audit.
- During the performance of the audit, the Audit Committee’s role should be one of oversight to ensure that there is progress in terms of the agreed timelines. In addition, the Audit Committee’s role includes:
  - Performing a high-level review of the financial statements and performance reports to be submitted for audit, including obtaining assurance from internal audit or other assurance providers that the financial statements and performance report have been prepared in accordance with the applicable frameworks and agree to the underlying schedules as prepared by management.
  - Engaging with management and the auditors to ensure that the documentation and explanations required by the auditors are being submitted in a timely manner.
  - Availing themselves to management and the auditors to resolve any disagreements or disputes, where required.

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- Once the audit is concluded, the audit outcomes are communicated to management through the management and audit reports. At this stage of the audit, the Audit Committee should:
  - Thoroughly review the management and audit report, focusing on areas of disagreement between the auditors and management, limitations placed on the audit, findings that are impacting the auditor's report and risks areas.
  - Discuss the findings with management and the auditors to identify the root causes and the remedies for compilation of the audit action plan.
  - Assist management, where necessary, on management representations, subsequent event matters and going concern issues.
  - Assess the findings from previous years as well as from other assurance providers for consistency and potential remedies.
  - Review the correspondence with respect to any material irregularities that have been raised and advise the Municipal Manager/Chief Executive Officer on the actions to be taken.

Comment on its evaluation of the controls, the financial statements and the performance report in the Audit Committee Report included in the annual report.

The Audit Committee Report plays a critical role in informing the view of users on the financial performance reporting of the public institutions and their general states of internal control in place.

It is of importance that the various stakeholders in the oversight and assurance process play their roles and hold each other accountable. The AGSA and the AC have a critical role to play in the public institutions to ensure that the services are delivered according to their stated mandates.

## 2.10 Combined Assurance

Combined Assurance can be defined as:

*“The planned approach to assess the extent and adequacy of assurance coverage on key organizational risks and reporting thereon to Senior Management, Audit Committee and the Governing Body.”*

A combined assurance model effectively co-ordinates the efforts of management and internal and external assurance providers, increases their collaboration and develops a shared and more holistic view of the Municipality’s/Municipal Entity’s risk profile. Combined assurance is about assurance providers (internal and external) working more closely together to ensure the following:

- Key outcomes of combined assurance;
- Assurance in the right areas is obtained;
- Assurance is obtained from the right resources; and
- Assurance is obtained in the most cost-effective way possible.

The combined assurance model classifies the risk landscape into types of risk with a potentially positive or negative effect on the ability of the Municipality/Municipal Entity to meet its strategy/objectives and protect or create value. It then goes on to formulate the approach to be followed in managing risk and the control and assurance continuum.

The Municipal Manager/Chief Executive Officer will ultimately decide on the most appropriate assurance provider for the identified risks. Where internal audit is identified as the most appropriate assurance provider, the Audit Committee must approve the scope of coverage and audit plan. Similarly, if external audit is to be relied upon for assurance, the Municipal Manager/Chief Executive Officer should inform them of this reliance to determine from the external auditors whether or not such reliance is appropriate from their work performed or will performed.

The Audit Committee is responsible to provide the oversight for combined assurance and will provide the Municipal Manager/Chief Executive Officer with a written assessment on the state of internal controls and risk management. The statement will be supported by the work performed by the Chief Audit Executive and the Internal Audit activity. The Audit Committee will provide approval of the combined assurance scope and coverage, provide oversight of the monitoring and consider the assurance provided. The Audit Committee should therefore determine who has the capacity and skills to drive Combined Assurance effectively.

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The foundation for combined assurance and the successful implementation of a combined assurance model rests on the quality of the risk management information and the clear mapping of the different lines of defense to the identified risks and controls. Poor risk definitions, missing critical risk information, no risk taxonomy and poor control mitigation information will negatively affect the implementation of combined assurance.

Implementing and maintaining a combined assurance model and framework for a Municipality/Municipal Entity should follow the following steps:

### **Step1 – Establishing the case for Combined Assurance**

- Gain high level understanding of the current/existing assurance profile.
- Establishing a risk universe
- Mapping the existing different lines of defense to the detailed risks and controls

### **Step2 – Doing an Assurance Reality Check**

- Identify all assurance providers.
- Perform an assessment of the assurance providers focusing on:
  - Independence and objectivity
  - Competency – level of professionalism and membership of a relevant professional body or institute
  - The quality of work provided is evident from an approved methodology, quality assurance process and references from other clients.
  - Assurance ranking
  - Impact and scope of assurance

### **Step3 – Detailed Risk and Assurance Mapping**

- Create a Combined Assurance Universe
- Identify gaps and duplications of assurance.

### **Step4 – Designing the Combined Assurance Model**

- Common risk language
- Update missing fields in the Assurance Map
- Assign assurance providers.
- Determine governance/management structures for reporting.

**Step5 – Continued Assurance**

- Internal audit assessment of adequacy of combined assurance
- Regular communication and reporting
- Audit Committee support, oversight and approval.

An effective combined assurance model should provide the Municipality/Municipal Entity with the following benefits:

- Co-ordinated and relevant assurance efforts focusing on key risk exposures across the production life cycle;
- Minimized operational and business disruptions;
- Comprehensive and prioritized tracking of remedial action on identified improvement opportunities/weaknesses;
- Improved reporting to the Council/Board and committees, including reducing the repetition of reports for review by the different committees;
- Possible reduction in assurance costs;
- Optimized assurance spends in that auditors are assisted in giving opinions on residual risk status, prevention of assurance fatigue, prioritize overlap between the lines of defense, and the prevention of possible 'blind spots;'
- The use of combined assurance to support the Audit Committee, Council and Board in making their control statements in the annual report and integrated report; and
- A comprehensive and prioritized approach to the tracking and testing of remedial actions on identified improvement opportunities, control weaknesses or significant inherent risk mitigations.

## 2.11 Managing the Audit Committee responsibilities

There are a number of mechanisms available that can assist Audit Committees to manage their responsibilities. These include:

- having an up-to-date charter;
- having a work plan indicating;
- conducting an assurance mapping exercise;
- establishing sub-committees;
- setting a forward meeting schedule—discussed further in Chapter 5, section 5.3.

### **Audit Committee charter**

Once the Municipal Manager/Chief Executive Officer and the Council/Board has determined the Audit Committee's responsibilities, these should be clearly outlined in the Audit Committee charter (see Part 3 for the model charter for Audit Committees).

The charter is a key document that clearly articulates the committee's terms of reference as endorsed by the Municipal Manager/Chief Executive Officer. Once established, the charter should be reviewed and, where necessary, updated each year. It may be appropriate to seek input from the Municipal Manager/Chief Executive Officer and Council/Board, to ensure the charter continues to meet the expectations of both the Municipal Manager/Chief Executive Officer and the Audit Committee. The committee could also seek feedback from the Chief Operating Officer, the Chief Financial Officer, The Head of Internal Audit, and external audit. Where the committee recommends changes to the charter, the Municipal Manager/Chief Executive Officer would be expected to condone the revised charter.

### **Audit Committee Work Plan**

An Audit Committee Work Plan enables Audit Committees to plan activities and meeting agendas ahead of each financial year. Forward planning by Audit Committees ensures compliance with the, MFMA, its supporting regulations and other guiding documents such as the King IV Report™. An example of an Audit Committee Work Plan for a Municipality/Municipal Entity is included in this Toolkit.



## **Assurance mapping**

To assist the Audit Committee to obtain a full understanding of a Municipality's/Municipal Entity's assurance arrangements, there can be benefit in the Audit Committee commissioning an assurance mapping exercise, also referred to as an Audit Universe. Recognizing that entities have a variety of assurance mechanisms and arrangements in place, such an exercise can be a useful way of obtaining a broad Municipality/Municipal Entity - wide perspective of the 'assurance landscape', assist in identifying any gaps or duplication in a Municipality's/Municipal Entity's arrangements, and can be used to complement the Municipality's/Municipal Entity's Risk Management Framework.

Mapping a Municipality's/Municipal Entity's assurance landscape should not be seen as an exercise that requires detailed analysis; broad judgements could be expected to be made following a review of existing documentation and discussions with relevant Municipality/Municipal Entity managers.

Such an assurance mapping exercise, when completed, can identify any key risks that are not being addressed by either internal audit or other assurance or review activity. An example of an assurance map for use by Audit Committees is contained in the toolkit.

## **Shared Audit Committees and Sub-committees**

Shared Audit Committee Structures between a local municipality and a district municipality (as an example) can be an effective method of addressing the specific challenges faced by smaller, rural municipalities. The composition of such a shared Audit Committee has to be well thought-through not to result in unnecessary large and costly structures that do not add value to the various municipalities they are serving.

The establishment of one or more sub-committees can also be an effective way for Audit Committees to manage their responsibilities. It is important to note that the formation of sub-committees should only be considered if they can be specifically warranted, and the Municipality/Municipal Entity can afford the additional cost associated with such a structure.

Sub-committees can be standing committees or established to assist in addressing particular issues for a defined period of time. Relevant considerations in deciding whether to establish a sub-committee include:

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- the benefit of dealing with substantive or complex matters and issues in more depth than is possible at full committee meetings, including detailed interaction with Municipality/Municipal Entity management. This might include, for example, issues of a more technical nature, such as the Municipality's/Municipal Entity's financial statements and information technology; the implementation of high-risk projects, programs, and/or activities; or where there is a considerable volume of documentation involved, such as large numbers of reports;
- the frequency with which the committee would be required to meet to effectively undertake its responsibilities in respect of particular matters or functions. For certain issues, the committee's involvement may be required to be more frequent than scheduled committee meetings;
- the capacity of the committee as a whole and individual members to understand particular matters—these could include, for example, an agency's financial statements or information technology risks and controls.
- other alternatives such as temporarily coopting a specialist/advisor to assist with the issue at hand, and
- the affordability of the alternative chosen.

**PART 3**

**3. MEMBERSHIP AND CONDUCT OF THE AUDIT COMMITTEE**

Having a chairperson and other committee members who have an appropriate mix of skills and experience relevant to the Municipality's/Municipal Entity's responsibilities is the key to an Audit Committee's effectiveness.

**3.1 Audit Committee Membership**

<b>Legislation</b>	<p>(5) An audit committee must—</p> <ul style="list-style-type: none"><li>(a) consist of at least three persons with appropriate experience, of whom the majority may not be in the employ of the municipality or municipal entity, as the case may be and</li><li>(b) meet as often as is required to perform its functions, but at least four times a year.</li></ul> <p>(6) The members of an audit committee must be appointed by the council of the municipality or, in the case of a municipal entity, by the council of the parent municipality. One of the members who is not in the employ of the municipality or municipal entity, must be appointed as the chairperson of the committee. No councillor may be a member of an audit committee.</p>
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The members of the Audit Committee must be appointed by the Council/Board of the Municipality/Municipal Entity or, in the case of a municipal entity, by the council of the parent Municipality/Municipal Entity. No councilor may be a member of the Audit Committee.

The number of members and the skills and experience of the Chairperson and other committee members will depend on a number of factors including:

- the nature of the Municipality's/Municipal Entity's responsibilities;
- the size, scale, location and diversity of the Municipality/Municipal Entity; and
- the complexity, nature and scale of the Municipality's/Municipal Entity's activities and systems; particularly its information technology systems.

It is better practice for the committee to include one or more members external and independent to the Municipality/Municipal Entity. Independence from Management and Freedom from any undue influence are essential qualities for independent members. Members of the Audit Committee should not have any executive powers, Management functions or delegated financial responsibility. To address this, measures should be put in place to assess the independence of Audit Committee members prior to and during appointment.

### 3.2 The Audit Committee Chairperson

The Chairperson of the Audit Committee plays a pivotal role in the overall effectiveness of the Audit Committee.

One of the members who is not in the employ of the Municipality/Municipal Entity or municipal entity, must be appointed as the Chairperson of the committee. The Chairperson of an Audit Committee may not be a political office bearer.

When appointing the Chairperson, particular consideration should be given to the personal qualities and abilities of the potential Chairperson to lead discussions, encourage participation of other members, and conduct meetings in a manner that demonstrates a desire to establish effective communications with all stakeholders. Below is a list of the qualities of a better practice Audit Committee Chairperson.

The Chairperson would be expected to:

- have the active support of, and maintain regular dialogue with the Municipal Manager/Chief Executive Officer and the Council/Board;
- ensure the committee undertakes its responsibilities as outlined in the committee charter;
- maintain an open and constructive relationship with senior management, internal and external audit, and other Municipality/Municipal Entity committees;
- have a clear understanding of the responsibilities of the committee, its position within the Municipality's/Municipal Entity's governance structure and the Municipality's/Municipal Entity's work, and maintain a dialogue with senior managers about the committee's work;
- arrange for committee members to maintain an up-to-date knowledge of the Municipality/Municipal Entity and its activities;
- be a good communicator who facilitates discussion and focuses on the important matters;
- effectively plan and manage committee meetings; and devote sufficient time to prepare for committee meetings and to engage with the Municipal Manager/Chief Executive Officer, the Council/Board, senior management and other stakeholders outside committee meetings.

It is also important for the Chairperson to have a good understanding of the Municipality/Municipal Entity and the Municipal Manager/Chief Executive Officer should take steps aimed to ensure the Chairperson is provided with sufficient initial and ongoing briefings and information about business developments.

### **Term of Office**

To enhance independence of the audit committee, the term of office for members must be strictly adhered to. The Chairperson should be appointed for a minimum of three years to ensure that he/she contributes most effectively and provides stability to the audit committee.

Other audit committee members should serve at least a minimum of three years with an option to renew for another three years, based on performance. Recruitment of members should be staggered to prevent a loss of knowledge and skills in the committee. Members should not be contracted continuously for a period exceeding six years. After serving continuously for six years, a cooling period of two years should be allowed before appointing the same member to the same Audit Committee.

A similar cooling off period is advised when an individual has been in the employment of the Municipality/Municipal Entity prior to being appointed as an independent member of the Audit Committee.

It is strongly encouraged that Audit Committee members limit the amount of Audit Committees they are involved in, to an amount that will allow them enough quality time to devote to their governance responsibilities such as understanding the organization they serve, preparing for Audit Committee meetings and adding value during meetings.

The recruitment process of new members should be concluded at least three months in advance of the expiry of existing members' term. The head of internal audit and the Municipal Manager/Chief Executive Officer must maintain records of audit committee member contracts and ensure recruitment is undertaken as mentioned above.

Rotation of members is encouraged as it enhances the independence of the audit committee. Members of the audit committee should not be contracted continuously for a period exceeding six years. After serving consecutively for six years, a cooling-off period of two years should be provided for, before appointing the same member to the same audit committee.

Members should be encouraged not to terminate their contracts until they have shared their knowledge with other new members. A committee member should give two months' notice prior to resignation.

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The committee members should have the opportunity to have an exit meeting with the Council/Board to discuss the reason for leaving and to provide feedback on their experience on the audit committee as well as any other issues. The date of resignation should be minuted by the secretariat of the audit committee. In order to perform its oversight functions in terms of the MFMA, municipalities and municipal entities must report details of all audit committee members, including the names, number of public institutions that they serve on as members, the term of office, date of appointment and termination. If audit committee members are removed from serving before the term the reasons for such termination must also be provided. This can be reported via e-mail to [mfma@treasury.gov.za](mailto:mfma@treasury.gov.za) and electronically via the Muni e-Monitoring web enabled system to be developed in this regard.

It is appropriate for a Deputy Chair to be appointed so the nominated member can act as Chair if the Chair is unable to attend meetings.

### **Preparation for Audit Committee Meetings**

The activities of the Audit Committee chairperson can be categorized into the following:

- Pre-Audit Committee meeting consultation.
- Identification of issues.
- Preparation for the Audit Committee meeting.
- Communication (during and after the Audit Committee meeting).

#### **Pre-Audit Committee meeting consultation**

The chairperson of the Audit Committee sets the standards and the values by which the Audit Committee will operate.

In order for the chairperson of the Audit Committee to:

- identify the issues for Audit Committee coverage;
- ascertain the contents of reports;
- set the agenda;
- determine the attendees and the topics they are to address – the Audit Committee normally consists of three or four members, the chairperson has the discretion to require others to attend (several invited attendees may not be required to attend throughout the meeting);
- ensure adequate time is allocated to address the key issues;

The Chairperson and audit committee may be required to meet separately with the internal auditors, external auditors, the secretary, Municipal Manager/Chief Executive

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Officer and Chief Financial Officer.

### **Identification of issues**

Prior to the Audit Committee meeting the Chairperson needs to extract and prioritize the issues obtained from the above, so that sufficient input can be obtained from the Audit Committee members during the meeting.

### **Preparation for the Audit Committee meeting**

The documentation for the Audit Committee needs to be distributed well in advance of the meeting e.g., a week to allow members to prepare.

Prior to the meeting, the reports that are being presented need to be studied for completeness, accuracy and relevance. This will assist the Chairperson of the Audit Committee in controlling the time spent on issues during the meeting and to ensure that there will be an outcome.

### **Communication (during and after the Audit Committee meeting)**

During the Audit Committee meeting, the Chairperson has to ensure that there is open and constructive discussion, a balance of contribution made between members and attendees and a conclusion on issues encouraged. An experienced secretary is required to record the meeting and take minutes. It is also important that management representation letters are received on relevant issues.

After the Audit Committee meeting, the Audit Committee Chairperson is required to:

1. Check and approve the draft minutes.
2. Follow-up regularly on the necessary issues prior to the next Audit Committee meeting.

Be clear about the decisions/mandates from the Audit Committee on the various issues.

3. Prepare a progress report for the Council/Board meeting and be prepared to be 'interrogated' by the Council/Board.
4. Identify those matters for which Council/Board accepts responsibility (preparation of interim and annual financial statements, fairness of financial statements, accounting policies, estimates, going concern, internal control, regulations, corporate governance statements, remuneration etc.).
5. Provide Council/Board with feedback on the quality of internal and external audit.

In MFMA Entities it is recognized that Audit Committees will generally include one or more members who are managers of the Municipality/Municipal Entity. As such, the appointment of an external member as Chairperson strengthens the actual and perceived independence of the committee. Sometimes, for example, in large and

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complex entities, it may be appropriate for the external to gain an understanding and experience of the Municipality/Municipal Entity it is recommended that a member to be elected as Chairperson first serve as a member of the Audit Committee, to gain the necessary knowledge and the respect and confidence of the Municipal Manager/Chief Executive Officer and other committee members, before assuming the role of Chairperson.



### 3.3 Personal qualities of Audit Committee members

In determining the composition of an Audit Committee, consideration of the personal qualities of members is critical. Committee members can be expected to possess all or the majority of the qualities listed below.

It would be expected that Audit Committee members have the ability to:

- act in the best interests of the Municipality/Municipal Entity as a whole;
- be proactive in identifying issues and risks that require further management attention;
- ask relevant questions, evaluate the answers and continue to probe for information until completely satisfied with the answers provided;
- encourage openness and transparency;
- work constructively with management to achieve continuous improvement within the Municipality/Municipal Entity;
- express opinions frankly, ask questions that draw out the key issues and pursue independent lines of enquiry;
- appreciate the Municipality's/Municipal Entity's culture and values, and a determination to uphold these values coupled with a thoughtful approach to the ethical issues that might be faced;
- display a professional approach to duties, including an appropriate commitment of time and effort; and
- convey technical matters to other members of the committee, where Audit Committee members have been chosen for particular technical skills.

Other attributes that will assist Audit Committee members to contribute to the committee's success include:

- good judgement
- objectivity and honesty
- a high level of ethics
- strong communication skills, and
- free from undue influence or intimidation

It is also expected that all committee members would have security clearances at a level commensurate with the security classification of documents accessed by members.

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The following individuals should not be considered for membership and/or independent membership of the Audit Committee:

- Councillors (not a member at all)
- Anybody in the employment of the Municipality/Municipal Entity (not an independent member)

### 3.4 Knowledge and expertise of Audit Committee members

Given the nature of the responsibilities of the Audit Committee, the Council/Board should appoint members who **collectively** possess broad business, financial management and public sector experience, and general knowledge of most or all of the areas listed below:

- the main activities of the Municipality/Municipal Entity including amounts others:
  - Engineering expertise
  - Event management understanding
  - Legal background
  - Environmental, Social and Governance (ESG) systems and reporting;
- risk identification, evaluation, and management;
- project and program management;
- information management and security;
- the operations of government and the public sector including information technology systems and controls;
- the roles of internal and external audit;
- the application of accounting, auditing and assurance standards;
- relevant legislative and other policy requirements of the Municipality/Municipal Entity;
- public sector and council structures including reporting requirements, financial and performance reporting;
- Corporate governance, internal control, compliance activities and fraud control; and
- Sustainability and business continuity.

It is important to the effective working of an Audit Committee that its members have sufficient Municipality/Municipal Entity knowledge. If the membership of the Audit Committee is relatively new, a higher proportion of members who know the organization can initially be helpful.

However, where a member's involvement with the Municipality/Municipal Entity is only through the Audit Committee, it is important that processes are established to help with the familiarization process and to keep members up-to-date with new developments. This is a responsibility of management that should be clearly articulated by the Municipal Manager/Chief Executive Officer, including the allocation of responsibility for the initial induction of external members and subsequent briefings on business developments.

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Given the specific responsibilities of the Audit Committee to advise the Municipal Manager/Chief Executive Officer and Council/Board on a Municipality's/Municipal Entity's financial statements, at least one member of the committee should have sound accounting or related financial management experience and/or qualifications, with a comprehensive understanding of accounting and auditing standards – specifically GRAP Standards. All members should have sufficient understanding of the Municipality's/Municipal Entity's financial reporting responsibilities to be able to contribute to the committee's consideration of the annual financial statements.

Additionally, there are other areas of Municipal operations that are specialized in nature, where the Audit Committee would benefit from having a member(s) with skills and experience in the specific business operation to assist the committee to meet its responsibilities. For example, where information technology systems have an important role in a Municipality's/Municipal Entity's business, it would be preferable for one member of the committee to have comprehensive information technology management experience and/or qualifications.

There may also be benefits in appointing a member from another Government entity as an external member, particularly where the entities have close working relationships or where a person has particular expertise in relation to a program or activity that is being implemented. Such appointments could be for shorter periods of time or could be in addition to the committee's normal membership.

The table below provides further guidance on the skills and experience of members that would enhance the Audit Committee representation and its performance to offer objective and quality advice.

<b>Skill Required</b>	<b>Metro</b>	<b>District with Services</b>	<b>District without Services</b>	<b>Local with Services</b>	<b>Local without Services</b>
Financial Management	✓	✓	✓	✓	✓
Legal	✓	✓	✓	✓	✓
Admin and Governance (i.e. Internal Audit, Risk Management, IT, Human Resources, Planning, etc.	✓	✓	✓	✓	✓
Performance Management	✓	✓	✓	✓	✓
Medical practitioner, Engineers (i.e. Civil, Electrical, Environment	✓	✓		✓	

### 3.5 Independence of Audit Committee members

The distinguishing feature of an Audit Committee is its independence. An Audit Committee is independent of the activities of management and this independence assists in ensuring that an Audit Committee acts in an objective, impartial manner free from any conflict of interest or inherent bias or undue external influence.

There are a number of ways to strengthen the committee's actual and/or perceived independence, as listed below.

Measures to strengthen the committee's actual and/or perceived independence include:

- the appointment of an external Chairperson. An external Chairperson can perform his or her role unencumbered by any management responsibilities and provides the opportunity for the Municipal Manager/Chief Executive Officer and Council/Board to receive advice and assurance from an independent perspective;
- the appointment of more than one external member;
- the appointment of committee members who exhibit an independence of mind in their deliberations and do not act as a representative of a particular area within the Municipality/Municipal Entity;
- having a rotation policy for Audit Committee members to enable new knowledge and experience to be introduced periodically to the committee and to allow the opportunity to include members from different parts of the Municipality/Municipal Entity over time;
- ensuring that the Audit Committee itself has no management responsibilities. Members who are staff of the Municipality/Municipal Entity, however, will have individual management responsibilities; and
- having policies in place to facilitate timely identification of changing relationships or circumstances that may affect the independence of Audit Committee members.

In view of the committee's responsibilities, as a general rule the Chief Operating Officer, Head of Corporate Services, the Chief Financial Officer, the Chief Information Officer, or the Head of Internal Audit should not be members of the Audit Committee, but it may be appropriate for them to attend meetings to participate and answer questions relating to their areas of responsibilities and as observers.

### 3.6 Ongoing support to members

To maximize members' contributions, particularly external members, support mechanisms should be in place to provide briefings and information on emerging business matters and risks. This may involve an increased commitment from management, the secretariat, and the Municipality/Municipal Entity generally.

There are several ways in which Municipalities can support their Audit Committees, including providing:

- an adequate secretariat service, initial induction and ongoing training;
- funding for expert advice, as required;
- reports from other Municipal committee meetings;
- support for senior line managers to attend Audit Committee meetings to discuss the business strategy, operations, and key risks for which they are responsible;
- assistance in arranging visits to Municipal locations and attending planning and other management events (such as strategic planning sessions, presentations by Municipal employees on topics or governance, finance, risks, controls, etc.); and
- appropriate meeting facilities and equipment – physical meetings.
- Facilitation of online meetings. It should be noted that the equipment and access to the internet required to attend online meetings will remain the responsibility of the individual Audit Committee members.

### 3.7 Induction of new Audit Committee members

The management and existing Audit Committee should have a formal process to induct new committee members that provides them with sufficient briefings and information to understand their responsibilities and the expectations of the Municipal Manager/Chief Executive Officer and the Council/Board about their role and performance.

The extent of each member's induction will vary depending on whether they are an internal or external member, their role (if any) within the Municipality/Municipal Entity and their particular knowledge and experience. As a minimum, all new members should be briefed by the Municipal Manager/Chief Executive Officer and the Chairperson of the Audit Committee and be introduced to the Chief Financial Officer, the Chief Information Officer, Head of Internal Audit and other senior managers and the external auditor.

The information provided to new members should be tailored to meet their individual requirements and can include the information listed below.

#### **Information for new Audit Committee members:**

The available information for new committee members should include:

- an outline of the Municipality's/Municipal Entity's governance framework and how the Audit Committee operates within that framework;
- the committee's charter and recent committee papers and minutes (including details of outstanding issues);
- other municipal committee charters;
- copies of the Municipality's/Municipal Entity's enabling legislation (where applicable), selected policies, such as Municipal Manager's/Chief Executive Officer's Instructions or equivalent, and a copy of the Municipality's/Municipal Entity's most recent financial statements;
- the Municipality's/Municipal Entity's annual report, corporate plan, code of conduct, business and risk management plans;
- a briefing (supported by relevant documentation) on the Municipality's/Municipal Entity's risk management framework, control, compliance, audit and external accountability arrangements, as well as details of current issues related to those topics;
- the latest annual report of the Municipality/Municipal Entity;
- the latest report from the Auditor General;

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- the internal audit charter, the strategic and annual internal audit plans, the committee's forward meeting schedule, and recent internal and external audit plans and reports; and
- this guiding manual.

When an external member joins the committee, it may be appropriate for more detailed information or presentations to be provided from various managers within the Municipality/Municipal Entity to assist the new member to gain the necessary understanding of the business. This could include site visits to assist in understanding the operations of the Municipality/Municipal Entity. See reporting requirements in paragraph 3.2.



### 3.8 Continuing education of Audit Committee members

The Chairperson of the Audit Committee, in consultation with the Municipal Manager/Chief Executive Officer, should monitor the level of further education of the committee and individual members in such areas as risk management, fraud control, program management, legal compliance, information management and security, and financial management and reporting.

Members of Audit Committees should be encouraged to continuously update their knowledge through:

- attendance at relevant seminars or courses;
- considering written material/guidance;
- attending or obtaining copies of presentations by the Chief Financial Officer, Chief Information Officer, Head of Internal Audit, and other senior managers;
- discussions and presentations from internal and external audit; and
- new legislation affecting the Municipality/Municipal Entity.

Information and training provided to Audit Committee members could be considered and should be tailored to the individual knowledge and expertise of the members and include developments in financial reporting as required by legislation, government requirements, and the accounting standards.

Effective Audit Committees will periodically request presentations from management and/ or subject-matter specialists on specific topics or developments to improve members' understanding of the Municipality/Municipal Entity and support ongoing training requirements for committee members. Presentations may cover topics such as:

- Municipal governance arrangements;
- specific policy or program initiatives; and
- business initiatives and risks.

It is ultimately expected of Audit Committee members to maintain continuous professional development requirements, in line with their respective professional obligations.

### 3.9 Change of Audit Committee members

It is important to balance stability with change in the membership of the committee to ensure there is consistency over time in its considerations, and to maintain a sufficient level of knowledge and experience on the committee.

It is better practice for the Municipal Manager/Chief Executive Officer to adopt a phased approach to the rotation of members to preserve an appropriate level of knowledge and expertise of committee members. To lessen the impact of the loss of an experienced member, the committee may also wish to have new members join the committee before exiting members depart. As this would result in a temporary increase in the number of members, such an option should be provided for in the committee's charter.

### 3.10 Transitional arrangements

In the public sector environment, with the possibility of changes to administrative arrangements and Municipal status, there is the potential that an Audit Committee may be replaced by a new committee, or that committee responsibilities may be transitioned to the Audit Committee of a new Municipality/Municipal Entity.

Where Audit Committee responsibilities are to be transferred to a new Audit Committee, it is the responsibility of the existing Chairperson to ensure that the status of all Audit Committee activities that may be relevant to the new committee is adequately documented and provided to the incoming committee in a formal report. In particular, any outstanding matters of high risk to the Municipality/Municipal Entity and outstanding audit recommendations should be brought to the attention of the new committee.

It is the responsibility of the committee Chairperson to ensure that an appropriate handover of responsibilities occurs on the appointment of a new Chairperson. An outgoing Chairperson should ensure that the new Chairperson is sufficiently briefed to assume the role of Chairperson. In particular, the outgoing Chairperson should brief the new Chairperson on any significant outstanding matters arising from internal and external reports and any major emerging risks facing the Municipality/Municipal Entity. The outgoing Chairperson would also facilitate a discussion between the Municipal Manager/Chief Executive Officer and the new Chairperson.

#### 4. Relationships with Key Stakeholders

An Audit Committee plays an important role in the governance structure of a Municipality/Municipal Entity. Municipal Managers/Chief Executive Officers and Councils/Boards are placing greater reliance on Audit Committees to provide them with independent assurance and advice in the areas of risk, control, and compliance in particular.

It is recognized that all Municipalities are different and each may have its own particular governance, risk management and control structures, and supporting policies and processes. As such, the provision of assurance and advice is to be determined within the context of each Municipality's/Municipal Entity's governance structure.

Audit Committees are required to provide a forum for communication between the Municipal Manager/Chief Executive Officer, the senior managers of the Municipality/Municipal Entity and the internal and external auditors of the Municipality/Municipal Entity.

Within a Municipality's/Municipal Entity's governance structure the Audit Committee should establish and maintain effective relationships with key stakeholders who influence and inform the responsibilities and operations of the committee. To achieve this, Audit Committees develop and maintain relationships through the Audit Committee meetings, and through working with key stakeholders outside of committee meetings.

Key Audit Committee stakeholders are:

- Council/Board;
- the Municipal Manager/Chief Executive Officer
- senior management including the Chief Financial Officer, Chief Information Officer, and Head of Internal Audit;
- management committees;
- internal and external audit;
- National Treasury;
- Provincial Treasury;
- The Department of Cooperative Governance and Traditional Affairs (COGTA);

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### **4.1 The Audit Committee and the Council/Board**

The Audit Committee has been legislated in to provide independent advice and oversight in terms of financial and non-financial matters in order to improve the effective functioning of organs of state. In addition, many audit findings can be prevented or mitigated through proper oversight by the Audit Committee.

The Audit Committee is a key contributor to good governance. It plays a crucial role in assisting the relevant Council/Board in discharging its responsibilities in overseeing financial and performance management, compliance with legal and other regulatory requirements and internal controls.

Key concerns identified by the Audit Committee that affect the effective functioning of the Municipality/Municipal Entity should be escalated to the Council/Board.

The following is a list of issues that should be escalated by the Audit Committee to the Council/Board and is not an exhaustive list:

<b>Area</b>	<b>Issue</b>
Risk and Control	<ul style="list-style-type: none"><li>• Summary of key risks facing the Municipality/Municipal Entity and how these are being addressed.</li><li>• Effectiveness of internal controls and any additional measures that should be implemented to address identified risks.</li></ul>
Assurance	<ul style="list-style-type: none"><li>• Significant external audit findings, recommendations and updated status thereof</li><li>• Significant internal audit findings, recommendations and updated status thereof</li></ul>
Finance	<ul style="list-style-type: none"><li>• Recommendation of draft financial statements for approval</li><li>• The Audit Committee's view on the financial position of the Municipality/Municipal Entity</li><li>• The appropriateness of the capacity of finance/treasury office. (Refer to the assessment tool provided in Part 4 of this Guide)</li></ul>
Compliance	<ul style="list-style-type: none"><li>• Any areas of non-compliance with relevant legislation and the status of the non-compliance.</li></ul>
Performance Management	<ul style="list-style-type: none"><li>• Audit Committee's findings and recommendations in line with service delivery and budget implementation plan</li></ul>

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General	<ul style="list-style-type: none"><li>• Results of any Audit Committee evaluations that have been conducted.</li><li>• Details of meetings and the number of meetings attended by each member of the Audit Committee</li><li>• Progress with any specific investigations delegated to the Audit Committee and their outcomes</li></ul>
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### **4.2 The Audit Committee and the Municipal Manager/Chief Executive Officer**

The Municipal Manager/Chief Executive Officer has a key role in supporting the effectiveness of the Audit Committee, and establishing active support amongst senior management is vital to the success of effective Audit Committees. As an Audit Committee is established to assist the Municipal Manager/Chief Executive Officer to discharge their responsibilities, it is important that the committee through its chairperson has an effective relationship with the Municipal Manager/Chief Executive Officer and key stakeholders. The committee Chairperson should develop a sound working relationship with the Municipal Manager/Chief Executive Officer that builds the respect and confidence that allow for effective communication.

Formal and informal reporting mechanisms should be in place with the Municipal Manager/Chief Executive Officer to facilitate the Audit Committee reporting on the committee's activities, key risk areas, and internal and external audit coverage. Reporting requirements should be summarized in the Audit Committee charter.

The Audit Committee should also prepare formal advice to the Municipal Manager/Chief Executive Officer on:

- the Municipality's/Municipal Entity's internal audit plans;
- the professional standards to be used by internal audit;
- any matter of concern, significant opportunities for improvement or good practices identified in internal and external audit reports;
- the preparation and review of the Municipality's/Municipal Entity's financial statements; and
- any advice the committee has about the Municipal Manager's/Chief Executive Officer's obligations under the MFMA.

For formal accountability purposes it is also expected that the committee would, at least once a year, report to the Municipal Manager/Chief Executive Officer on its operation and activities during the year. The report could include those matters listed below.

The committee's report could be expected to include:

- a summary of the work the committee performed to discharge its responsibilities during the preceding year. For example, its responsibilities for reviewing the financial statements for sign-off by the Municipal Manager/Chief Executive Officer;
- a summary of the committee's assessment of the Municipality's/Municipal Entity's risk and control framework, including the Municipality's/Municipal Entity's business continuity preparedness, disaster recovery, fraud control, information security, and

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details of emerging risks facing the Municipality/Municipal Entity;

- a summary of key issues the committee dealt with during the year, such as significant internal and external audit findings and recommendations, including a summary of the status of audit recommendations, any significant risk incidents and any breaches of legislation by the Municipality/Municipal Entity; and
- details of meetings, including the number of meetings held during the relevant period, and the number of meetings attended by each member.

For many committees the most effective communication with the Municipal Manager/Chief Executive Officer is for the Audit Committee Chairperson to brief the Municipal Manager/Chief Executive Officer following each committee meeting, which may be orally or in writing, however, written brief is recommended to ensure that appropriate evidence and tracking of resolutions is maintained.

In recognition of the legislative requirement to establish an Audit Committee, consideration should be given to reporting the Audit Committee's activities in the Municipality's/Municipal Entity's annual report. This could include membership details, and a summary of the main issues the committee addressed during the year.

The committee should be able to report to the Municipal Manager/Chief Executive Officer on any other matter it considers of sufficient importance to do so. In addition, at any time an individual committee member may request a meeting with the Municipal Manager/Chief Executive Officer.



### 4.3 The Audit Committee and senior management

To be effective, the Audit Committee must be independent from management and free from any undue influence. Independent Members of the Audit Committee should not have any executive powers, management functions or delegated financial responsibility.

As Audit Committees are generally advisory in nature, the members' understanding of the difference between the responsibilities of the committee and the decision-making functions of management must be clear.

The approach the Audit Committee adopts in its interaction with senior management will have a direct bearing on the effectiveness of the committee. If the committee demonstrates a positive culture of continuous improvement, rather than a punitive culture, the committee is more likely to effectively fulfil its role.

The Municipality/Municipal Entity can contribute to a strong relationship with the Audit Committee by arranging for the external Audit Committee Chairperson to attend selected management meetings as an observer. This would assist the Audit Committee to maintain an up-to-date understanding of the Municipality/Municipal Entity. It can also assist the Chairperson to maintain constructive relationships with senior management. Attendance at such meetings is also an opportunity for the Chairperson to brief senior management on Audit Committee activities.

The Audit Committee can contribute to strong relationships with management by providing executive managers with a brief summary of the issues dealt with at each meeting, including details of actions to be undertaken by management. This simple process can heighten the visibility of the committee and be a practical way to demonstrate that the Municipal Manager/Chief Executive Officer takes the responsibilities of the committee seriously.

It is important that senior managers have a good understanding of the Audit Committee's responsibilities. Municipality/Municipal Entity managers should adopt an open and constructive attitude in their dealings with the committee as a whole and with individual members. They are to be forthcoming in identifying any areas of potential weakness or risk that could be considered in developing the internal audit plan and be constructive when interacting with or addressing issues the Audit Committee or internal and external audit raise.

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The Audit Committee should be alert to opportunities for senior management representatives to attend meetings, to facilitate further discussion on action to implement audit recommendations, or to explain why any recommendation has not been addressed appropriately or in a timely way. Presentations or attendance by senior managers at an Audit Committee can be useful in building trust and effective communication links between the committee and management, particularly where the Municipality/Municipal Entity is managing significant risks and where internal and/or external audit have made significant recommendations. Presentations from senior management should align with the Audit Committee's responsibilities.

### **Follow-up of audit recommendations**

An important responsibility of the Audit Committee is to review actions taken by management to implement internal and external audit recommendations. The action management takes should accord with the responses and timeframes documented in the audit reports that have been agreed by the Municipality/Municipal Entity and reviewed by the Audit Committee. One way the committee can effectively monitor management's implementation of audit recommendations is to have a standing agenda item requiring a listing of outstanding recommendations to be tabled at scheduled meetings. To assist the committee to assess management's performance in implementing audit recommendations, internal audit should maintain an appropriate process for monitoring and reporting on the status of agreed internal or external audit recommendations or agreed recommendations from parliamentary committees or other review bodies. Outstanding recommendations should be prioritized for action by the Audit Committee.

Effective committees will arrange for officers responsible for implementing significant audit recommendations to attend committee meetings to enable the committee to obtain direct feedback on progress in implementing the recommendations.

Where necessary, the Audit Committee should advise the Municipal Manager/Chief Executive Officer on action it considers necessary to address significant issues in internal and external audit reports. This can be done through a written report or summary provided to the Municipal Manager/Chief Executive Officer or through discussions between the Municipal Manager/Chief Executive Officer and the committee Chairperson.

### **Chief Operating Officer**

Chief Operating Officers (COOs) are generally responsible for a broad range of administrative functions that will include matters such as risk management and legislative compliance, that are within the purview of the Municipality's/Municipal Entity's Audit Committee.

In these circumstances, there may be an inherent conflict of interest in the COO being a member of the Audit Committee. It is therefore better practice for the COO not to be a member of the Audit Committee but could be invited as an observer, to provide briefings to the committee on business developments.

### **Chief Financial Officer**

The relationship between the Chief Financial Officer (CFO) and the Audit Committee is an important one in the context of the committee's financial statement and internal control responsibilities. The Audit Committee should put arrangements in place that provide for the CFO to advise the committee in a timely manner of all significant accounting and financial reporting issues that may affect the financial statements and the underlying systems of internal control, and for the committee to seek assurance that any such issues are being addressed in a timely manner. In addition, the Audit Committee can provide the CFO with advice and assistance on matters relating to the preparation of the Municipality's/Municipal Entity's financial statements.

To avoid potential conflicts of interest it is better practice for the CFO to be invited to attend Audit Committee meetings as an observer, rather than as a committee member.

### **Chief Information Officer**

Effective lines of communication are required between the Chief Information Officer (CIO) and the Audit Committee, as information and communications technology are an important part of the Municipality's/Municipal Entity's business operations and will often be an area of risk requiring careful review. Ideally, the CIO will be able to clearly explain specialized information technology system matters to the committee, or a members will possess sufficient expertise to enable the committee to fully understand the CIO's advice and any potential implications.

To avoid a potential conflict of interest, it is better practice for the CIO to be invited to attend Audit Committee meetings as an observer, rather than as a committee member.

### **Head of Internal Audit**

Establishing a sound working relationship with the Head of Internal Audit will assist the Audit Committee to meet its responsibilities, particularly those relating to internal audit that include reviewing internal audit plans and reports, and resourcing of the internal audit function.

It would be expected that the Audit Committee is consulted on the appointment, dismissal and performance review of the Head of Internal Audit.

To avoid a potential conflict of interest it is better practice for the Head of Internal Audit to be invited to attend Audit Committee meetings as a standard invitee, rather than as a committee member.

#### 4.4 The Audit Committee and other committees

The relationship between the Audit Committee and other committees in a Municipality's/Municipal Entity's governance framework is important to enable the committee to effectively meet its responsibilities. For example, if a Municipality/Municipal Entity has a Risk Committee and/or an IT Steering Committee, the Audit Committee should be aware of the responsibilities and meeting outcomes of these committees. Relationships with other committees such as the Disciplinary Board, Risks Management Committee and Municipal Public Accounts Committee (MPAC) should also be considered. This would minimize the chance of the Audit Committee duplicating work done by the risk committee and/or identifying gaps that require attention.

To facilitate the relationship between the Audit Committee and the work of the various management committees within a Municipality/Municipal Entity, it is important that there is a timely and free flow of information between the committees.

Effective Audit Committees will have formal mechanisms to facilitate such an exchange of information. These mechanisms could include:

- periodically obtaining briefings from representatives of other committees; and/or
- having the minutes of each management committee distributed to the other committees as a standing item on each committee's agenda.

#### 4.5 The Audit Committee and internal audit

The relationship between the Audit Committee and internal auditors is central to enabling the committee to meet its responsibilities. As such, the relationship between the Head of Internal Audit and the Committee is an important one. Internal audit is functionally responsible to the Audit Committee and works for the committee through its Head.

Reports by internal audit provide the Audit Committee with a key source of information on the Municipality's/Municipal Entity's performance. Maximizing the value of internal audit requires that open lines of communication be established and maintained between internal audit and the committee.

##### **Strategic and Annual Internal Audit Work Plans**

The Audit Committee should review and provide advice to the Municipal Manager/Chief Executive Officer on the adequacy of Strategic and Annual Internal Audit Work Plans.

The nature of the Internal Audit Strategic Audit Plan will be commensurate with the size and complexity of each Municipality/Municipal Entity, as well as the Municipality's/Municipal Entity's risk profile, and the extent of the Municipality's/Municipal Entity's investment in the internal audit function. In developing this plan consideration should be given to the Municipality's/Municipal Entity's goals and objectives, internal and external risks, the work of other review activities or functions, stakeholder expectations and internal audit business objectives and management strategies. There should be sufficient flexibility in the Internal Audit Strategic Audit Plan to accommodate additional audits that the Municipal Manager/Chief Executive Officer may commission from time to time. The Annual Internal Audit Work Plan should be reviewed periodically by the Audit Committee to re-confirm the relevance and priority of audit topics.

Where the internal audit function is outsourced, particular attention should be given to potential conflicts of interest when considering the appointment of a service provider or the proposed Internal Audit Strategic Audit Plan. It is important to fully consider any restrictions placed on the scope of audit coverage, and to help the committee gauge the level of coverage of particular areas over time the committee would consider previous audit activity in the areas identified for audit.

Once approved, the Audit Committee should consider the mechanisms for communicating the approved plan to relevant stakeholders, including the Municipal Manager/Chief Executive Officer and senior management. Municipalities might consider placing the approved Internal Audit Strategic Audit Plan on their intranet to make it available to all stakeholders and staff.

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On an ongoing basis during the year, the Audit Committee would review the internal audit's progress in carrying out the approved work program. This review would take into consideration:

- reasons for any adjustments to the scope of the review, particularly when requested by Municipal Manager/Chief Executive Officer; and
- changes to the timing of assignments and reasons for any delays against the approved timetable.

### **Internal audit resourcing**

An important responsibility of the Audit Committee is to be satisfied that there are sufficiently skilled internal audit resources available to undertake the approved internal audit work program, including providing support for, and input to, the committee. Consideration of internal audit resources would include a periodic review of the model of internal audit the Municipality/Municipal Entity uses, that is, in-house, outsourced or co-sourced, and the range of resources required, to assess whether they are appropriate for the Municipality/Municipal Entity. Considerations would include the Internal Audit Strategic Audit Plan and the audits required to be conducted. If the committee decides that internal audit resources are not adequate, the Chairperson of the Audit Committee should formally raise the committee's concerns with the Municipal Manager/Chief Executive Officer.

Where the internal audit function is outsourced, it would be expected that the committee would provide input to the statement of requirements developed as part of a tender process and provide advice on the appointment of the service provider. In particular, the committee should be alert to any potential conflicts of interest involving possible service providers. Where internal audit is provided in-house, the committee would be expected to contribute to the selection process of the Head of Internal Audit, particularly in determining the qualities expected of the appointee.

### **Internal audit reports**

In addition to regular, informal communication between internal audit and the Audit Committee, the committee should receive regular reports, in an agreed format, from the internal audit on the results of their work. This should include management's response to internal audit recommendations and other suggestions for improvement. Responses from management should be clear and concise and should include:

- whether management agrees or disagrees with the finding and recommendation. If there is disagreement, identify the reasons; and

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- identifying the specific position or work area responsible for implementing the recommendation; a brief outline of the action to be taken; and the timeframe for implementation.

### **Audit Committee members-only session with internal audit**

It is better practice to have a private session with internal audit, at a scheduled meeting(s) during the year that provides an opportunity for the committee to raise issues, ask questions and seek feedback from the internal auditor without management present. This supports the recognition of the independent role of internal audit.

### **Review the performance of Internal Audit**

Each year the Audit Committee should review the performance of internal audit. The Audit Committee should also commission a periodic external review of internal audit.

Standard 1312 of the International Standards for the Professional Practice of Internal Auditing requires independent external assessments to be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization.

In evaluating the effectiveness of internal audit, the Audit Committee needs to assess the effectiveness of internal audit against agreed performance criteria, including:

- compliance by internal audit – be it in-house, outsourced, or co-sourced – with its agreed charter or plan/scope and level of performance;
- the overall comprehensiveness of the internal audit plan and its relationship with the strategic objectives of the business;
- delivery of timely internal audit services in accordance with the plan; and
- the competency of internal audit staff and adequacy of resources to achieve the scope as outlined in the plan. This may require outsourcing certain specialists' skills not available in the internal audit function.

The Audit Committee should, on an annual basis, request a review of internal audit performance from various sources including management and the external auditor.

The internal audit activity of the Municipality/Municipal Entity should also report on their level of conformance with the International Standards for the Professional Practice of Internal Auditing, on an annual basis. The report should be a result of the Quality Assurance and Improvement Program developed and maintained by the internal audit activity. In terms of the Institute of Internal Auditors' quality assurance review process the following criteria should be used to indicate the level of conformance with the International Standard for the Professional Practice of Internal Auditing:



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<b>Conformance Rating</b>	<b>Description/Criteria</b>
General Conformance	For individual standards, that the internal audit activity conforms to the requirements of the standard (e.g., 1000, 1010, 2000, 2010, etc.) or elements of the Code of Ethics (both Principles and Rules of Conduct) in all material respects.
Partial Conformance	For individual standards, the internal audit activity is making good faith efforts to conform to the requirements of the standard (e.g., 1000, 1010, 2000, 2010, etc.) or elements of the Code of Ethics (both Principles and Rules of Conduct) but falls short of achieving some major objectives.
Does not Conform	For individual standards, the internal audit activity is not aware of, is not making good faith efforts to conform to, or is failing to achieve many/all of the objectives of the standard (e.g., 1000, 1010, 2000, 2010, etc.) and/or elements of the Code of Ethics (both Principles and Rules of Conduct).

Refer to “Evaluation of the Internal Audit Function” in Part 4 of this manual for further guidance.

#### 4.6 The Audit Committee and external audit

External auditor independence in the public sector does not present the same challenges for an Audit Committee as in the private sector, given the legislative requirements supporting the independence of external audit and the Auditor General.

The external auditors should have a standing invitation to all Audit Committee meetings. To further enhance an effective relationship between the Audit Committee and external audit, there should be a mechanism in place to facilitate an open and frank exchange of information between committee members and external audit throughout the year. Audit Committee members should be in a position to be able to openly discuss matters of interest in a sensitive manner with the external auditors in any areas covered by the Committee's functions.

##### **External audit coverage**

The Audit Committee should be briefed on the proposed external audit coverage and fully consider:

- the financial statement areas of audit focus, the assessment of Municipality/Municipal Entity risks, and associated fees (where applicable);
- proposed performance audit coverage;
- any potential overlap with internal audit coverage;
- the impact on internal Municipality/Municipal Entity resources and management effort; and
- the engagement letter as discussed with management.

It is expected that the Audit Committee would review all substantive correspondence from external audit about planned audits, audits in progress, and completed audits, and extend a standing invitation for the external auditor to be present at each committee meeting for all agenda items (with the exception of members-only sessions that the Committee may hold periodically). Being present at each meeting as an observer allows the external auditor to obtain a better understanding of a Municipality's/Municipal Entity's operations and risks and, among other things, enables external audit to provide a status report on audit activity and to provide input for the committee's deliberations.

The Audit Committee should obtain a briefing from external audit on the results of their audit of the financial statements. The committee should also be briefed periodically on the results of any performance audits or assurance reviews undertaken.

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Where external audit utilizes the services of a third party service provider, an Audit Committee may wish to consider the steps necessary to gain assurance that there is no conflict of interest with respect to the work undertaken by a third party service provider. In some cases, this could include the Chairperson, or other nominated member, attending presentations by tenderers during the tender process. Audit Committees should also obtain periodic assurance that any new contractual arrangements between the Municipality/Municipal Entity and the third party service provider do not result in conflicts of interest.

Each year, the Audit Committee should review its relationship with external audit and any third party service provider engaged by external audit. The review should include providing feedback on the service provided, and on the effectiveness of communication and reporting between external audit, the committee, internal audit and management.

### **Audit Committee members-only session with external audit**

It should be standard practice for the external auditor to meet alone with the committee members at least once a year.

Having a private session with external audit representatives provides an important opportunity for the committee to raise issues, ask questions and seek feedback from external audit without internal audit or management observers present.

### **Response to issues raised by the Auditor General**

Section 131 of the MFMA requires that a Municipality/Municipal Entity must address any issues raised by the Auditor-General in an audit report in the format of an Audit Action Plan.

The effectiveness of an Audit Action Plan is measured through the successful implementation of timely and appropriate actions, must prevent a recurrence of the audit findings in subsequent audits and translate into an improvement in the audit opinion.

A web-enabled audit action plan system, known as the Financial Management Capability Maturity Model (FMCMM) has been developed to ensure more rigorous engagement between Provincial and National departments and municipalities contributing towards ongoing improvements in audit outcomes. Using this tool will benefit municipalities in the following ways:

- The standardized format ensures that all necessary information is included in the audit action plan.
- An approval process is embedded in the system that incorporates management, the CFO, Internal Audit, Audit Committee, and the Municipal

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Manager/Chief Executive Officer.

- It allows for multiple users to access and work on the audit action plan at the same time.
- It provides for e-mail alerts once sections are completed and supports efforts of National and Provincial Treasuries to provide support, advice, comments and recommendations.
- In-year and ongoing progress in implementation of the audit action plan can therefore be monitored in real time by all users through all stages. The progress tracking is done through the audit action plan Dashboards which track the resolution of the number of audit findings and users are able to extract reports on progress to address identified internal control deficiencies.
- Quality assurance is also ensured as internal audit units are required to confirm that the resolution of the findings was adequate before an action plan status can change to “Complete.”
- The need to report separately to different stakeholders is obviated as treasury officials have access to real time information.

The online system gives users the ability to develop an action plan to resolve audit outcomes and track progress towards improvements. The Auditor-General’s audit and management reports are the main drivers for the population of the audit action plan, which will follow an approval process involving key stakeholders from the CFO, Internal Auditor, Audit Committee, and Council/Board.

In addition, repeat findings and prior year proposed solutions are identifiable for special attention by stakeholders to expedite interventions when and where needed, both at the planned action phase, as well as at the implementation phase.

The system also stores past audit action plans, and this accumulation of knowledge would enable users to trace actions taken in previous years, and follow-up on corrective actions relating to prior year findings which have failed to adequately address and resolve the finding. In so doing, the system will assist in the identification of root causes of repeat findings so that appropriate actions may be introduced that will effectively resolve these findings.

The reporting functionality of the system supports improved decision making by working collaboratively with managers so that they actively report real time information and evidence where recommendations have been addressed and this will help reduce the amount of time and effort needed to follow-up. The filter mechanism allows a selection of reported information to be extracted such that only relevant information is included in reports destined for use by the various oversight structures, such as Council/Board, MPAC and Audit Committees.

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Dashboards provide high level overviews of trends and progress in implementing the audit action plan.

The web-enabled audit action plan links to priorities to improve audit outcomes, encompasses all areas of the Municipality/Municipal Entity and municipal entity that have specific responsibilities in resolving audit findings, will inform training and capacitation plans, and strengthen the role of the Internal Audit and Audit Committee when performing assurance checks.

**5. Conduct of the Audit Committee**

The operation of an Audit Committee will be enhanced by having an effective Chairperson; the committee being supported with appropriate secretariat arrangements; meetings being well planned and conducted efficiently; committee members having appropriate access to Municipality/Municipal Entity staff and information; and actual and potential conflicts of interest being effectively managed.

Efficiencies can also be achieved in some circumstances if small Municipalities are able to meet their legal obligations by utilizing the members and support services of larger Audit Committees.

In managing Audit Committee activities, it is important for Municipalities to meet all relevant legislative and policy requirements, particularly in relation to the appointment of external members.

## 5.1 The role of the Chairperson in the conduct of the Audit Committee

The Chairperson plays a pivotal role in the effective functioning of any committee, with particular responsibilities to set the tone and direction of the committee's deliberations.

The Chairperson is the most important appointee. The Chairperson needs to have expertise and experience in governance and to bring personal qualities and independence to the role that will openly and effectively involve all those the Audit Committee needs to work with.

### **Audit Committee Chairperson responsibilities:**

The Audit Committee Chairperson's responsibilities will generally be to:

- recommend to the Municipal Manager/Chief Executive Officer, the appointment of Audit Committee members, without undue influencing;
- assist committee members to maintain a good understanding of the Municipality's/Municipal Entity's objectives, business needs, risks and priorities;
- settle the agenda for each meeting with the committee secretariat;
- lead discussion and encourage the participation of other members, and focus the committee's deliberations on the most important issues;
- seek the input of observers or other experts to maximize their contribution to the deliberations of the committee;
- summarize discussion outcomes and actions, including assigning responsibility and timeframes for actions;
- report formally and informally to the Municipal Manager/Chief Executive Officer and the Council/Board;
- attend formal and informal meetings with senior management, the Chief Financial Officer, the Chief Information Officer, the Head of Internal Audit and external audit as required; and
- arrange for a periodic review of the effectiveness of the Audit Committee against its charter.

To be effective, it is important that the Audit Committee operates in an environment of co-operation and trust. This is generally achieved when the Audit Committee Chairperson promotes an open and cooperative relationship with senior management, other Municipality/Municipal Entity committees, and the internal and external auditor.

## 5.2 Committee secretariat

It is important that the Audit Committee is appropriately supported by effective secretariat arrangements. It is expected that the secretariat works closely with the Chairperson to assist in ensuring that:

- all committee papers are of an appropriate standard and are available to committee members sufficiently in advance of meetings to allow members appropriate timeframes for review and consideration;
- minutes are maintained of committee meetings; and
- members are kept abreast of key developments in the Municipality/Municipal Entity.

Secretariat responsibilities would generally include:

- liaising with the committee Chairperson to prepare meeting agendas;
- coordinating the preparation and circulation of committee papers within agreed timeframes;
- preparing minutes of committee meetings, including action points arising from meetings and details of actions to be undertaken by management;
- facilitating the approval of minutes of previous meetings;
- supporting the Chairperson in the preparation of Audit Committee reports to the Municipal Manager/Chief Executive Officer;
- maintaining a record of when members' terms of appointment are due for renewal or termination;
- ensuring that new members receive appropriate induction training, and that all members are supported in identifying and participating in ongoing training;
- recording of the attendance of members of the Audit Committee;
- highlighting matter arising from previous meetings; and
- managing expenditures relating to the Audit Committee's operations.

The secretariat also has an important role in assisting the Audit Committee to maintain communication channels between the internal and external auditors and to assist the committee in keeping the Municipal Manager/Chief Executive Officer informed of the Audit Committee's activities.



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The secretariat can also assist the Audit Committee by providing members with progress reports from internal and external audit, as outlined below:

- A progress report from the Head of Internal Audit summarizing:
  - work performed (and a comparison with work planned);
  - key issues emerging from internal audit work;
  - significant changes to the organization's Risk Register;
  - management responses to audit recommendations; and
  - any resourcing issues affecting the delivery of internal audit.
- A report from external audit summarizing work done—financial statements, performance audits, cross-agency audits, better practice guides—and emerging findings.

### 5.3 Audit Committee planning

The preparation of a forward meeting schedule that includes the dates, location, and agenda items for each meeting, and covers all the committee's responsibilities as outlined in the committee's charter can assist the meeting in undertaking these responsibilities in a structured and timely manner. This can also be referred to as the Audit Committee Work Plan.

Some committees see benefit in arranging a separate planning meeting at which the work of the committee for the next 12 months can be discussed, priorities identified through discussions with relevant Municipality/Municipal Entity managers, and any changes to the committee's functions and responsibilities identified.

## 5.4 Audit Committee meetings

### **Number and timing of meetings**

Audit Committee meetings are generally spread across the year with one meeting timed to match the Municipality's/Municipal Entity's financial statements timetable. While the number of meetings and their duration will vary depending on the range and complexity of the committee's responsibilities, it would be expected the committee would meet at least four times a year, together with a special meeting to consider the Municipality's/Municipal Entity's financial statements. Committees are increasingly seeing this meeting schedule as a minimum requirement in an environment where Municipal Managers/Chief Executive Officers are seeking a greater level of assurance and advice from Audit Committees, combined with the increasing complexity of Municipality/Municipal Entity responsibilities. Committees should carefully consider whether they have scheduled sufficient meetings to ensure they are able to fully discharge their responsibilities. For example, where significant issues arise during the year in relation to high-risk programs or activities for which the committee has review responsibilities, committees should consider the benefits of scheduling additional meetings.

The Audit Committee charter should require the Chairperson of the committee to hold a meeting if asked to do so by the Municipal Manager/Chief Executive Officer, and for the Chairperson to decide if a meeting is required if requested by another member. It may at times be appropriate to deal with issues out-of-session to keep committee meetings focused.

### **Attendance at meetings**

It is expected that internal and external auditor representatives will be invited to participate in all agenda items at each committee meeting as observers. The committee may also ask management representatives to attend committee meetings for particular agenda items.

As the Municipal Manager/Chief Executive Officer would not be expected to be on the committee, they may be invited to attend committee meetings to participate in specific discussions or provide strategic briefings. Some committees provide the Municipal Manager/Chief Executive Officer with a standing invitation to attend committee meetings.

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As committee members should be appointed for their particular skills and experience, it is generally accepted that members are not permitted to send proxies if they are unable to attend meetings. However, arrangements may be required to address circumstances where management representatives on the committee are absent for lengthy periods or act in positions that would generally exclude them from membership.

### **Quorum**

A quorum should consist of a majority of committee members. In committees which have more than one external member, particularly in MFMA entities, it is better practice for a quorum to include at least one external member. If a quorum is not present at a meeting, the meeting may proceed with the understanding that it is subject to ratification by the ensuing Audit Committee meeting, which would require a proper quorum.

### **Meeting agenda**

Audit Committee meetings should be well structured and managed. The efficient running of each meeting can be assisted by:

- the Audit Committee Chairperson approving the agenda;
- the agenda ensuring important and/or contentious matters being discussed ahead of more routine business;
- the meeting starting and finishing on time;
- members agreeing the priority to be devoted to each agenda item at the commencement of each meeting;
- each member being able to be briefed before each meeting by the secretariat on the major issues to be discussed; and
- meeting papers being prepared and presented in an agreed form.

Some committees find it beneficial to set time aside before each meeting for the Audit Committee members to discuss the agenda and any issues they wish to discuss in more depth with management. This 'committee-only' time also allows Audit Committee members to discuss issues with other members before management representatives and other observers join the meeting.

As discussed previously, it is important that the Chairperson and other committee members interact with senior managers outside committee meetings so that a Municipality/Municipal Entity can benefit from advice and insights that committee members can provide, and to assist committee members in keeping abreast of business developments.

**Minutes of Audit Committee meetings**

Minutes of Audit Committee meetings should be clear and concise, providing a summary of the outcomes and actions with clear responsibilities and timeframes attached. Draft minutes should be distributed to the Chairperson within one week of the meeting for clearance, and to committee members within two weeks of the meeting. In addition to the minutes, it is good practice for the Audit Committee to provide the Municipal Manager/Chief Executive Officer with a brief summary of the issues dealt with at each meeting including details of actions to be undertaken by management.

## 5.5 Managing conflicts of interest

To strengthen the Audit Committee's actual and perceived independence, the committee should develop protocols for dealing with actual or perceived conflicts of interest.

These protocols could include the following arrangements:

- Each year, members of the Audit Committee declare potential, perceived or real conflicts of interest they may have in relation to their role, and be required to update them regularly during the financial year. External members should consider past employment, consultancy arrangements and related party issues; and
- At the beginning of each Audit Committee meeting, members should raise any conflict of interest issues and, where required, the member should be excused from the meeting for the relevant agenda item(s).

Where members or observers at Audit Committee meetings are deemed to have a real or perceived conflict of interest it may be appropriate that they are excused from committee deliberations on the issue where a conflict of interest exists. Details of potential or actual conflicts of interest declared by members and action taken should be appropriately minuted. During online meetings it is preferable that the affected member leave the online meeting and not simply be muted.

These protocols should help reinforce the importance of committees identifying and managing, where necessary, actual and potential conflicts of interest.

**5.6 Access to staff and information**

The Audit Committee charter should provide the committee and individual members, where agreed by the Chairperson, with the authority to access Municipality/Municipal Entity staff and information held by the Municipality/Municipal Entity that is relevant to the committee's responsibilities. In exercising this authority, the committee and individual members should at all times be alert to the risk of interfering in the executive authority of management. In practice, the requirement to separately access staff and information would be expected to be on an exceptional basis.

To enhance the committee's independence and its capacity to obtain a full appreciation of relevant issues, the Audit Committee charter would also be expected to authorize the committee to seek independent professional advice, as and when required.

### 5.7 Audit Committee arrangements in small Municipalities

A number of Municipalities required to establish an Audit Committee are very small in terms of population density. There can be practical difficulties associated with such entities establishing a viable and effective Audit Committee. There may be merit in these entities exploring ways of entering into contractual or other cooperative arrangements with other Municipalities within their portfolio to meet, in a cost-effective way, their legislative obligation to establish an Audit Committee. This could be done, for example, by sharing members and support services with another committee.

In circumstances where a committee acts as an Audit Committee for more than one Municipality/Municipal Entity, it is important that each committee has its own charter and membership and separate minutes be kept for each committee and provided to the Municipal Manager of each Municipality/Municipal Entity. The committee should also consider if any issues regarding potential conflicts of interest arise as a result of sharing information among entities.



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### **5.8 Contractual arrangements and remuneration**

When accepting an appointment to serve on an Audit Committee, external members should ensure that the contractual arrangements established clearly outline their role and the terms and conditions of their appointment. This should include any requirements relating to hours to be worked, indemnity insurance, signing of conflict of interest declarations, remuneration and any specific requirements, so members fully understand their obligations.

#### **Audit Committee Members' Remuneration**

The members of the Audit Committee shall be remunerated for time spent in attendance of Audit Committee meetings. The Municipality/Municipal Entity may utilize the rates provided by the National Treasury, from time to time. Should the Municipal Manager/Chief Executive Officer deem it necessary, he or she can, in consultation with the Council/Board, determine other remuneration, provided that the charter properly defines time and cost.

External committee members should be remunerated at a level that reflects the time it takes to effectively meet their responsibilities. Allowance should be made for the particular skills and expertise the member will bring to the committee, and the time required for meeting preparation and attendance at meetings and interaction with management outside committee meetings. Recognition should also be made for the additional responsibilities of the Chairperson.

Remuneration will only be applicable to officials employed outside the public service. No remuneration for participating in Audit Committees will be payable to officials employed at national, provincial and local government and any organ of state.

The rates for remuneration of external Audit Committee members, as determined by the South African Institute of Chartered Accountants in consultation with the Auditor General are published as follows:

	Per Day	Per Hour
Chairperson	RX	RX
Member	RX	RX

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The reimbursement of all members for travel expenditure must be determined in accordance with the approved Council/Board policy or the rate per kilometer as published and updated by the National Department of Transport.

The Municipal Manager/Chief Executive Officer, in consultation with the Chief Financial Officer, is required to approve the reimbursement of all travel expenditure for members of the Audit Committee based on the above mentioned or make alternative arrangements to pay for modes of travel to such meetings, in terms of Council/Board policy.

The Chairperson and members of the Audit Committee, including members who are employed in the public service, will be required to complete all particulars of their respective travel to and from the venue of the Audit Committee meetings.

In the event that an official from one Municipality/Municipal Entity is requested to serve as a member of an Audit Committee of another Municipality/Municipal Entity, such senior official must first obtain written consent from the Municipal Manager before accepting such nominations. The remuneration discussion early will apply.

### **Insurance arrangements**

When considering the issue of external members' professional indemnity insurance cover, Municipalities would be expected to take into account the generally advisory nature of the committee and any risks to the Municipality/Municipal Entity of relying on the advice or actions of an individual member, as distinct from the committee as a whole.

In this regard, it would be important to recognize that the advice provided to a Municipality/Municipal Entity and the exercise of certain functions such as the signing of committee minutes and the provision of a report to the Municipal Manager/Chief Executive Officer is in a person's capacity as a member of the Audit Committee, rather than as an individual.

## **6. AUDIT COMMITTEE PERFORMANCE**

A structured and formal evaluation of an Audit Committee's performance can help ensure the committee delivers on its charter and can help the committee continuously enhance its contribution to the Municipal Manager/Chief Executive Officer. The evaluation may be a self-assessment, with input from key stakeholders, or involve facilitation or review by an external party. Self-assessment is generally considered to be a sufficient method of evaluation for governance committees. The 360-degree performance assessment tool is a popular method to obtain feedback on performance from all directions. It can assist to enhance performance, improve relationships and foster accountability.

## 6.1 Audit Committee performance assessment

The performance assessment process should involve an assessment of the committee as a whole and may extend to an assessment of the performance of individual members.

An effective committee will complete an assessment annually to evaluate its performance against its charter and involve input from:

- The Municipal Manager/Chief Executive Officer on the quality and timeliness of assurance and advice provided by the committee;
- individual committee members on the effectiveness of the committee in meeting its responsibilities including planning, the decision-making process, and the relationship and quality of communication with stakeholders;
- key stakeholders, for example, senior management, the Chief Financial Officer, the Chief Information Officer, external audit and National / Provincial Treasury, on the effectiveness of the committee's stakeholder management;
- other committees that the Audit Committee interacts with;
- the Auditor General; and
- Provincial Treasury.

The results of the assessment should be provided to the Municipal Manager/Chief Executive Officer, who should consider the findings and any recommendations of the assessment and, if required, ensure appropriate action is taken to enhance the committee's performance.

### **Assessment of an Audit Committee member's performance**

In an MFMA entity, consideration of an executive member's performance on an Audit Committee will, in practice, be undertaken as part of his/or her overall performance assessment.

It would be expected that the Chairperson of the Audit Committee would undertake a performance assessment of external members where an extension of the member's tenure is being considered, taking into consideration whether the member has:

- a good understanding of the Municipality's/Municipal Entity's business;
- a good understanding of, and commitment to, the committee's responsibilities;
- displayed the ability to act objectively and independently and made a constructive contribution to the work of the committee; and

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- displayed a willingness to devote the time required to prepare for, and participate in, committee meetings.

### **Acting on Audit Committee Member Non-performance**

The Chairperson of the Audit Committee should evaluate the performance of individual committee members and the Council/Board should evaluate the performance of the Chairperson. Input from management of the Municipality/Municipal Entity, Internal and External Auditors could also form part of the assessment process.

Audit committee members may be dismissed by the Municipal Council/Board under certain circumstances (e.g. where an on-going conflict of interest exists, where a member has not performed to expectations etc.).

The official dismissal processes of the Municipality/Municipal Entity should be adhered to by the Accounting Officer and Municipal Council/Board when an Audit Committee member is being dismissed. The dismissal of a member should be performed by the Municipal Council/Board and the outcome of the dismissal process should be in writing.

The dismissal should be supported by a well-documented non-performance of the committee member against clear and agreed-upon performance criteria. Criteria to be considered would include:

- Expertise and know-how;
- Inquiry attitude, objectivity and independence;
- Judgement;
- Knowledge of local government and its objectives;
- Understanding of and commitment to the committee's duties and responsibilities;
- Devotion of time in order to participate effectively in the committee;
- Timely responses;
- Attendance of meetings.

Reports containing information regarding the performance and / or non-performance of an Audit Committee or Audit Committee members must be submitted to National and Provincial Treasury who may express a view or make further recommendations to assist with the effective functioning of the Audit Committee.

## **PART 4**

### **7. Tools, Guidelines and Templates**

#### **7.1 Audit Committee Legal Status**

An Audit Committee (and each of its members) should act only within the scope of the committee's specified functions and responsibilities and in accordance with any instruments of appointment, authorization and delegation.

Audit Committee members are expected to exercise their powers and perform their functions with due care, skill and diligence and act in good faith in the best interests of the Municipality/Municipal Entity and for a proper purpose.

Audit Committee members are personally liable for any breach of their duties in respect of actions taken by them and may be held liable for a breach of their duties or legal obligations, and for contraventions of the general law. However, an Audit Committee member's potential liability, in respect of their committee duties, will generally be no greater than that:

- to which they would be subject in respect of their general duties within that Municipality/Municipal Entity (for a member that already holds another executive or non-executive position within the same Municipality/Municipal Entity); or
- to which they would be subject in the course of providing such services on a normal contractual basis (for an external committee member).

MFMA entity Audit Committee legislative and policy requirements:

(Please take note that changes to the legislation may occur. Audit Committees, Councils and Accounting Officers must regularly identify changes to the MFMA and address the potential impact of these changes on the functioning of the Audit Committee.)

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Legislation	Requirements of the MFMA
<p>MFMA Act 56 of 2003 Chapter 14 General Treasury Matters</p>	<p>Section 166</p> <p>(1) Each Municipality and each municipal entity must have an Audit Committee.</p> <p>(2) An Audit Committee is an independent advisory body which must -</p> <ul style="list-style-type: none"> <li>(a) advise the municipal council, the political office-bearers. the accounting officer and the management staff of the Municipality, or the board of directors, the accounting officer and the management staff of the municipal entity on matters relating to- <ul style="list-style-type: none"> <li>(i) internal financial control and internal audits;</li> <li>(ii) risk management;</li> <li>(iii) accounting policies;</li> <li>(iv) the adequacy, reliability and accuracy of financial reporting and information</li> <li>(v) performance management;</li> <li>(vi) effective governance;</li> <li>(vii) compliance with this Act, the annual Division of Revenue Act and any other applicable legislation;</li> <li>(viii) performance evaluation; and</li> <li>(ix) any other issues referred to it by the Municipality or municipal entity;</li> </ul> </li> <li>(b) review the annual financial statements to provide the council of the Municipality or, in the case of a municipal entity. the council of the parent Municipality and the board of directors of the entity, with an authoritative and credible view of the financial position of the Municipality or municipal entity, its efficiency and effectiveness and its overall level of compliance with this Act, the annual Division of Revenue Act and any other applicable legislation;</li> </ul>

- (c) respond to the council on any issues raised by the Auditor-General in the audit report;
- (d) carry out such investigations into the financial affairs of the Municipality or municipal entity as the council of the Municipality, or in the case of a municipal entity, the council of the parent Municipality or the board of directors of the entity, may request; and
- (e) perform such other functions as may be prescribed.

(3) In performing its functions, an Audit Committee –

(a) has access to the financial records and other relevant information of the Municipality or municipal entity; and

(b) must liaise with -

(i) the internal audit unit of the Municipality; and

(ii) the person designated by the Auditor-General to audit the financial statements of the Municipality or municipal entity.

(4) An **Audit Committee** audit must -

(a) consist of at least three persons with appropriate experience. of whom the majority may not be in the employ of the Municipality or municipal entity, as the case may be and

(b) meet as often as is required to perform its functions, but at least four times a year.

(5) The members of an **Audit Committee** must be appointed by the council of the Municipality or, in the case of a municipal entity, by the council of the parent Municipality. One of the members who is not in the employ of the Municipality or municipal entity, must be appointed as the Chairperson of the committee. No councilor may be a member of an **Audit Committee**.

(6) A single **Audit Committee** may be established for –

(a) a district Municipality and the local municipalities within that district Municipality; and

(b) a Municipality and municipal entities under its sole control.



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<p>MFMA Act 56 of 2003 Chapter 12 Financial Reporting and Auditing</p>	<p>Section 121</p> <p>(1) Every Municipality and every municipal entity must for each financial year prepare an annual report in accordance with this Chapter. The councilor of a Municipality must within nine months after the end of a financial year deal with the annual report of the Municipality and of any municipal entity under the Municipality’s sole or shared control in accordance with section 129.</p> <p>(2) The purpose of the annual report is –</p> <p>(a) To provide a record of the activities of the Municipality or municipal entity during the financial year to which the report relates;</p> <p>(b) To provide a report on performance against the budget of the Municipality or municipal entity for that financial year; and</p> <p>(c) To promote accountability to the local community for the decisions made throughout the year by the Municipality or municipal entity.</p> <p>(3) The annual report of the Municipality must include –</p> <p>(j) any recommendations from the Municipality’s Audit Committee</p> <p>(4) The annual report of a municipal entity must include –</p> <p>(g) any recommendations of the Audit Committee of the entity of its parent Municipality;</p>
<p>MFMA Act 56 of 2003 Chapter 14 General Treasury Matters</p>	<p>Section 165 – Internal audit unit</p> <p>(1) Each Municipality and each municipal entity must have an internal audit unit, subject to subsection (3).</p> <p>(2) The internal audit unit of a Municipality or municipal entity must –</p> <p>(a) Prepare a risk-based audit plan and an internal audit program for each financial year;</p> <p>(b) Advise the accounting officer and report to the Audit Committee on the implementation of the internal audit plan and matters relating to –</p> <p>(i) Internal audit;</p> <p>(ii) Internal controls;</p> <p>(iii) Accounting procedures and practices;</p> <p>(iv) Risk and risk management;</p> <p>(v) Performance management;</p> <p>(vi) Loss control; and</p> <p>(vii) Compliance with this Act, the annual Division of Revenue Act and any other applicable legislation;</p>

*Table 2: MFMA entity Audit Committee legislative and policy requirements*

7.2 Example of Assurance Map for Audit Committee

Entity business risks (taken from an entity's risk management plan)	Source and level of assurance provided					Overall assessment of level of assurance	Is level of assurance adequate?
	Work area	Work area	Management committees	Internal audit	Other assurance activities		Yes/No
Failure to recruit, develop and retain sufficient skilled staff to sustain core service delivery at required levels.	low	moderate	(Human Resource Management) moderate	low	-	moderate	Yes
Failure to assess, monitor and appropriately manage key organizational requirements including resource and budget management in a changing business environment.	low	low	(Executive Board) moderate	moderate	(External review) low	moderate	Yes
Failure to adequately manage the entity's complex contractual arrangements	low	moderate	(Executive Board) moderate	Low	-	moderate	No
Ineffective and/or inappropriate management of information.	low	low	(Information Management) moderate	moderate	-	moderate	Yes
Diminished stakeholder confidence, loss of confidence by the minister or government.	moderate	low	(Executive Board) moderate	low	-	moderate	No
Failure to comply with legislative requirements.	moderate	low	(Executive Board) moderate	moderate	(Certificate of Compliance) high	high	Yes
Ineffective financial management	moderate	moderate	(Finance) moderate	moderate	(Audit Committee) High	high	Yes
Failure to work with or manage implementation partners.	moderate	low	(Executive Board) low	low	-	low	No
Unable to sustain efficient business processes and develop desired delivery solutions to meet business needs.	low	moderate	(Executive Board) moderate	low	-	moderate	No

The level of entity assurance and advice provided on the entity business risks —high, moderate, low. The level of assurance provided will depend on the extent to which the controls in place and other arrangements address the business risk.

Table 3: Example of Assurance Map for Audit Committee

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### **7.3 Checklists and Templates**

Part 4 of the Guide consists of: a number of checklists relating to particular areas of responsibility of Audit Committees; a checklist to assist in guiding discussions with the Municipal Manager/Chief Executive Officer; a template forward meeting schedule and self-assessment questionnaire.

Completed checklists should be retained in the Audit Committee's records to evidence the committee's deliberations.

#### **Templates**

The templates provided, as part of this guide, are generic in nature and the Audit Committee, through the Chairperson of the Audit Committee, and the Municipal Manager/Chief Executive Officer, should use these templates as guides for developing their own Audit Committee governing documents.

The following templates, checklists and guidelines are contained as annexures to this guide:

#### **Templates**

<b>DOCUMENT NAME</b>	<b>DOCUMENT NUMBER</b>
Audit Committee Terms of Reference/Charter - MFMA	PSAUC1
Audit Committee Work Plan	PSAUC2
Audit Committee Induction Pack	PSAUC3
Internal Audit Charter Template	PSAUC4
Audit Committee Self-Assessment Template	PSAUC5
Audit Committee Competency Framework	PSAUC6
Internal Audit Effectiveness Assessment	PSAUC7
Audit Committee Assessment of the Finance Function	PSAUC8

## 8. Supporting and Guiding Documentation

The list of documents indicated below will assist the Audit Committee in its effective functioning and will contribute to the achievement of the Audit Committee's roles and responsibilities.

<b>DOCUMENT NAME</b>	<b>DOCUMENT NUMBER</b>
Audit Committee Terms of Reference/Charter - MFMA	PSAUC1
Audit Committee Work Plan	PSAUC2
Audit Committee Induction Pack	PSAUC3
Internal Audit Charter Template	PSAUC4
Audit Committee Self-Assessment Template	PSAUC5
Audit Committee Competency Framework	PSAUC6
Internal Audit Effectiveness Assessment	PSAUC7
Audit Committee Assessment of the Finance Function	PSAUC8

END OF GUIDE

All comments to be provided via email to [mfma@treasury.gov.za](mailto:mfma@treasury.gov.za)