



Internal Audit Methodology

Ubuhlebezwe Municipality

Internal Audit Activity



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1. Introduction and Background

In terms section 62(1)(c) of the Municipal Finance Management Act (Act no 56 of 2003)(MFMA), the Accounting Officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure that the municipality has and maintains effective, efficient and transparent systems

- (i) of financial and risk management and internal control;
- (ii) of internal audit operating in accordance with any prescribed norms and standard.

Section 165 of the Municipal Finance Management Act no 56 of 2003 states that, the Internal Audit Activity must –

- (a) Prepare on an annual basis a risk-based audit plan and an internal audit programme of the municipality for each financial year;
- (b) Advise the Accounting Officer/Municipal Manager through reports to the Audit Committee on the implementation of the internal audit plan and matters relating to
 - Internal Audit;
 - Internal Controls;
 - Accounting Procedures and Practices;
 - Risk and risk management;
 - Performance management;
 - Loss control; and
 - Compliance with MFMA, Division of Revenue Act (DORA) and any other applicable legislation.

- (c) Perform such other duties as may be assigned to it by the Accounting Officer/Municipal Manager

This manual has been prepared to provide guidance on the standards and procedures to be followed in the performance and documentation of every internal audit engagement conducted by the Ubuhlebezwe Internal Audit Activity, with the primary objective of driving consistency and quality in the internal audit work.

The objectives as well as the procedures to be followed for each section are explained with reference to the Standards for the Professional Practice of Internal Audit and international good practice.

Internal audit engagements are currently documented on TeamMate and manually.

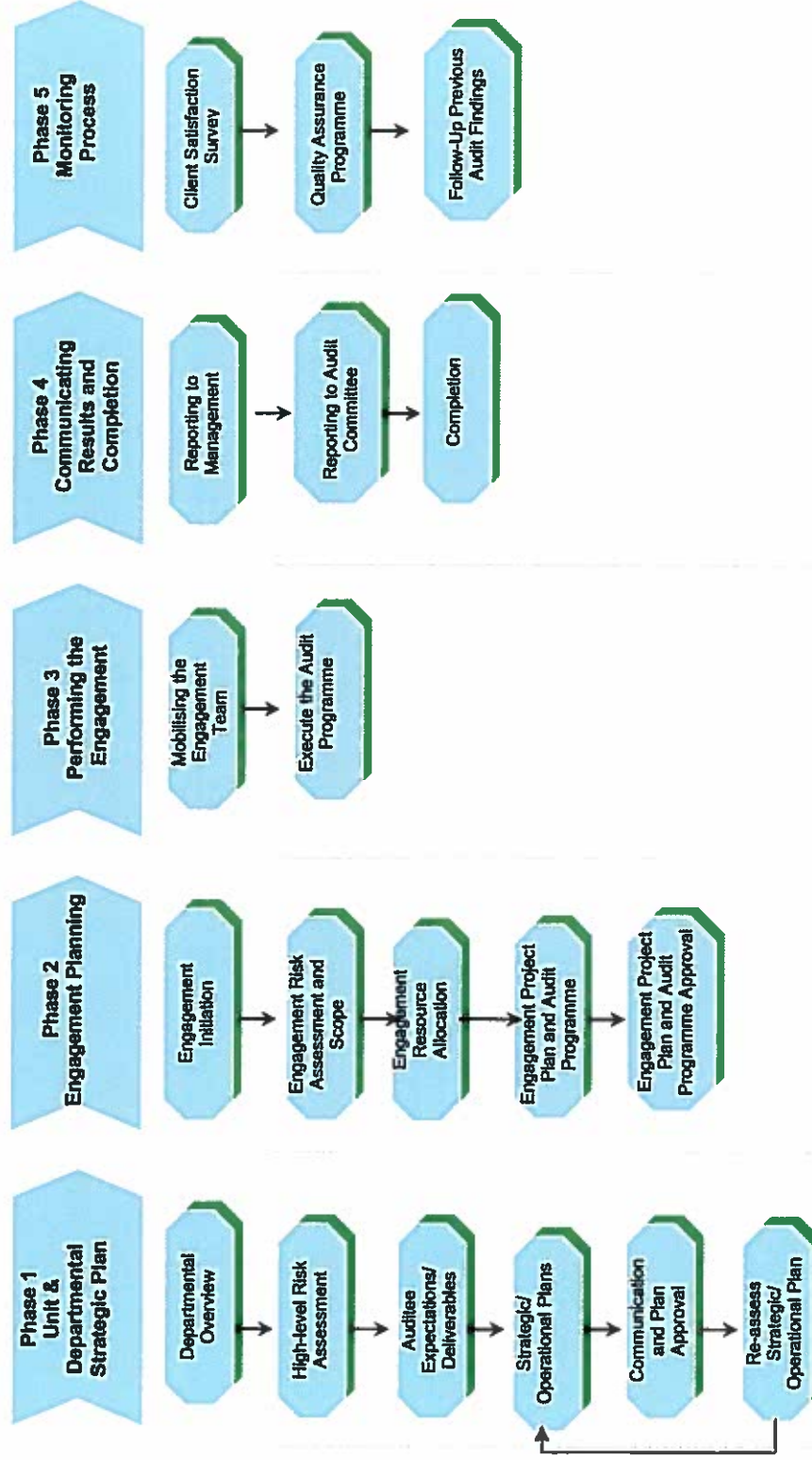
Internal audit staff should bear in mind that this Internal Audit Methodology Manual is a guideline and can be modified to suite peculiar circumstances. Authority and guidance should be sought from the Manager: Internal Audit prior to deviating from this guideline.



UBUHEBEZWE MUNICIPALITY: INTERNAL AUDIT ACTIVITY

Baseline Internal Audit Engagement

(Mandate: MFMA Section 165, IA Charter, AC Charter, SPPIA, Code of Ethics)



Documentation, Review & Supervision, Quality Assurance, Independence, Objectivity, & Professional Care



2. Phase 1: Municipality's Strategic Planning

2.1 Introduction

International Standards for the Professional Practice of Internal Auditing:

2010 –Planning

"The chief audit executive should establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organization's goals".

Strategic planning is critical for determining that the audit plan reflects the most appropriate internal audits to address client's expectations and the risk profile of the organisation.

The primary purpose of the internal audit strategic plan is to outline in detail to management and the Audit Committee the areas which will be reviewed by internal audit so that they are able to form a view on whether the planned coverage and scope (recognising not all areas can be addressed with finite resources) is sufficient to meet their needs.

The Strategic and Operational internal audit plans are prepared in terms of section 165 of the MFMA:

- A rolling three-year strategic internal audit plan based on the assessment of key areas of risk for the municipality, having regard to its current operations, those proposed in its strategic plan and its risk management strategy;
- An annual internal audit plan for the first year of the rolling three-year strategic internal audit plan.

2.2 Municipal Overview

Overview:

The overall objective of the Municipal Overview is to gather background information about the municipality, its objectives, its structure to achieve the objectives, the risks and opportunities that may prevent or facilitate the achievement of these objectives and the processes that exist to monitor and manage the related risks.

Key objectives:

- Develop an understanding of the municipality's structure, key programmes, etc.
- Develop a preliminary understanding of municipality's objectives/ risks.
- Where applicable, develop an understanding of and validate with management, its structure and organisation for delivering departmental objectives.
- Where applicable, develop an understanding of and validate with management the effectiveness of its identification, capture, evaluation and management of risk.
- Develop an understanding of the corporate culture of the municipality and the control environment.
- Define the audit universe.

Key steps:

1. Review public information.
 - This should include a review of applicable Regulations, Acts, etc.
2. Review Municipal information.
 - This should include a review of the municipality's strategic plan, organisation chart, internal management reports, budget statement and previous internal



- and external audit reports and risk and control register (from the Risk & compliance office).
3. Obtain a preliminary understanding of the municipality's objectives, risks and control environment.
 - This should be obtained through management interviews and a review of the documentation listed in 2 above.
 4. Document the audit universe.
 - In arriving at the audit universe, consideration should be given to the municipality's programmes and/or processes, such that the audit universe is practical and supports an efficient audit process.
 - Planning Section – Municipality's Overview
 - Planning Section – Audit Universe

Templates
Audit Universe

2.3 High-Level Risk Assessment

International Standards for the Professional Practice of Internal Auditing:

2110 – Risk Management

"The internal audit activity should assist the organization by identifying and evaluating significant exposures to risk and contributing to the improvement of risk management and control systems."

2010.A1 – Planning

"The internal audit activity's plan of engagements should be based on a risk assessment, undertaken at least annually. The input of senior management and the board should be considered in this process".

Overview:

The overall objective of the high level risk assessment is to obtain an understanding of the key risks facing the municipality, as well as the related controls, in order to develop an internal audit plan that is appropriately focused on the areas of more significant risk.

A risk assessment should be developed at the onset of the planning process and updated on a continual basis going forward.

The risk assessment and subsequent development of the risk register for the municipality is facilitated by the Risk & compliance office assisted by KZN Provincial Treasury. Management remains ultimately responsible for the identification and management of risk. The outcome of the risk assessment is used as a key input into the development of the strategic internal audit plan.

A high-level overview of the Enterprise Wide Risk Management Framework is included in Appendix A.

Key objectives:

- Obtain an understanding of the risks facing the municipality.
- Identify the significant risks that require an internal audit response.

Key steps:

1. Obtain the Municipality's risk register (risks and controls) from the Risk and Compliance office.
 - The top 10 risks, rated on an inherent risk basis, should be considered in the strategic planning process.



2. Group/classify risks and map to the audit universe.

- Planning section – Risk assessment.

Template

Risk assessment mapping.

2.4 Auditee Expectations/Deliverables

International Standards for the Professional Practice of Internal Auditing:
2010 –Planning

“The chief audit executive should establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organization’s goals”.

Overview:

The overall objective is to ensure that there is a clear and complete understanding of the internal audit mandate, terms of reference, and management and/or the Audit Committee’s expectations.

Key objectives:

- Understand the Audit Committee and the Accounting Officer’s expectations.
- Understand the internal audit mandate and terms of reference.
- Determine the expected balance between key control testing and value-added audit effort and the nature and extent of testing.
- Define nature, timing and content of internal and external deliverables.

Key steps:

1. Review of Internal Audit Charter and previous Audit Committee minutes.
 - In order to understand the broad mandate assigned to internal audit and to glean information on the Audit Committee preferences, the Internal Audit Charter and minutes of previous meetings should be reviewed with a view to informing the current strategic planning process.
2. Conduct a preliminary planning meeting with the Head of Department.
 - A high level understanding of key expectations for the internal audit should be obtained and the strategic and engagement planning process, high-level timeframes and key deliverables should be agreed.
3. Define management engagement and deliverable expectations.
 - The engagement expectations as well as the nature, timing and content of the key deliverables should be reassessed on an ongoing basis.
4. Develop the proposed high-level timeframes for key deliverables.
5. Define applicable reporting templates.

Note: These steps should be completed in sufficient detail to enable the completion of the relevant sections in the Strategic Plan Template.

- Planning Section – Summary of auditee expectations
- Planning Section – Summary of key deliverables

Templates

- ✓ Minutes of meeting with HOD
- ✓ Schedule of key expectations (Management and the Audit Committee)
- ✓ Schedule of key deliverables
- ✓ Internal Audit Report



2.5 Strategic /Operational Plans

International Standards for the Professional Practice of Internal Auditing:

2200 – Engagement Planning

"Internal Auditors should develop and record a plan for each engagement, including the scope, objectives, timing and resource allocation."

Overview:

The overall objective of the Strategic Plan is to document the results of the planning steps so far and to obtain management's agreement to the scope of the work planned.

A three year strategic rolling plan (Strategic Plan) should be prepared based on the key areas of risk for the department, having regard to its current operations, those proposed in its strategic plans and its risk management strategy.

In addition to the consideration of key risk areas, the Strategic Plans also need to incorporate the auditee's expectations for other types of work. For example:

- Requests from management to perform specific engagements;
- Compliance audits;
- Rotational coverage of programmes/locations over a defined cycle of time;
- Assisting the external auditors;
- Coverage of transversal issues as advised by the Risk office ;
- Follow-up audits;
- Legislated audits.

The creation of the Strategic Plan is an exercise seeking to achieve balance between risk priorities, auditee expectations, time and available resources.

Key objectives:

- Align risk assessment results and the auditee expectations (Strategic Plan).
- Provide a summary of the risk assessment and a plan for audit coverage over a 3 year period (Strategic Plan).
- Provide a basis for discussions with management, necessary to obtain approval for the planned work (Strategic Plan).
- Establish the current year plan (Operational Plan).
- Provide basis for engagement planning in phase 2 (Operational Plan).
- Establish basis for assigning resources (Operational Plan).

Key steps:

1. Using the risk assessment mapping (output from 2.3), determine the auditable areas/engagements required.
 - Consideration should be given to the relative riskiness of the auditable area/engagement, based on the number and rating of risks assigned to it.
 - All Top 10 risks should be selected for internal audit coverage.
2. Using the summary of auditee expectations, determine the auditable areas/engagements required.
3. Develop a high level scope for each auditable area/engagement as identified in 1 and 2 above.
4. Determine the resources and time available for the year (July – June) based on the productive time of staff.
 - The resources allocated to the cluster should be determined.
 - The standard time available (excluding annual leave, study leave, administration and training) from each resource should be determined.



- The budget available for insourcing skills to increase capacity and/or specialist skills should be determined.
5. Develop the draft Strategic and Operational plan.
 - It is important to achieve a balance between the auditee's expectations, risk priorities and other stakeholder requirements when developing the plan. This is an area of professional judgement and should take into account all of the information gathered in the planning process so far.
 - The resources and estimated hours should be allocated to each auditable area/engagement.
 - The estimated timing of engagements over the financial year should be set.
 - The impact of resource limitations on the planned work should be highlighted in the draft Strategic/Operational Plan such that the Head of Department can prioritise the internal audit focus.
 6. Prepare the draft Strategic/Operational plan.
 - The draft Strategic/Operational plan should be prepared by the Internal Auditor and reviewed by the Audit Manager.
 7. Approve the draft Strategic/Operational plan.
 - The Audit Committee should approve the draft Strategic/Operational plan.
 8. The Auditor General is given an opportunity to comment on the draft Strategic/Operational plan during the Audit Committee meetings.

➤ Planning – Draft Strategic/Operational plan

Templates

- ✓ Strategic/Operational plan

2.6 Communication and Approval of the Plan

International Standards for the Professional Practice of Internal Auditing:

2020 – Communication and Approval

"The chief audit executive should communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive should also communicate the impact of resource limitations."

Overview:

The draft Strategic/Operational plan should be submitted to the Accounting Officer and management for comment. The Audit Committee should approve the final plan prior to its execution.

Key objectives:

- Obtain management's buy-in to the planned work.
- Identify expectation gaps.
- Obtain agreement on balance between compliance auditee's expectations, risk priorities and other stakeholder requirements.

Key steps:

1. Review the draft Strategic/Operational plan.
 - The draft Strategic/Operational plan should be reviewed by the Manager: Internal Audit prior to discussion with management.
2. Discuss the draft Strategic/Operational plan with management.



- The meeting should, be attended by the Accounting Officer, Chief Financial Officer and the rest of the management committee, and all attendees are provided an opportunity to provide comments on the draft Strategic/Operational plan.
 - Where resource limitations are likely to impact the planned scope of the internal audit work, management should be requested to prioritise the internal audit coverage.
 - Update the Strategic/Operational Plan with any changes that may be required arising from the discussions above.
3. Obtain final Strategic/Operational plan approval as follows:
- Manager: Internal Audit – evidenced by signature on plan.
 - Accounting officer of a Municipality - evidenced by signature on plan.
 - Presented to the Audit Committee by the Audit Manager.
 - Audit Committee Chairperson - evidenced by signature on plan.

Note: The original final approved signed plan should be kept with the Manager: Internal Audit.

4. Obtain the approved Strategic/Operation Plan before the engagement planning commences.
5. Monitor the execution of the plan on an ongoing basis.
- Throughout the year the engagement team should monitor execution of the audit plan, and prepare periodic updates for management and the Audit Committee highlighting progress to date, modifications to the plan, significant findings and trends etc.

➤ Planning – Final strategic/operational plan

Templates

- ✓ Minutes of meeting with of Head of Departments/and MANCO regarding discussion and approval of Strategic/Operational plan.
- ✓ Strategic/Operational plan

2.7 Re-Assess Strategic/Operational Plan

Overview:

The overall objective is to recognise changes in objectives /risks within the Strategic/Operational Plans and update the Strategic/Operational Plan accordingly.

Key objectives:

- Reassess and modify the approved Strategic/Operational Plan during the year as a result of changes in the business, changes in objectives, or changes in risk factors.
- Discuss modifications to the Strategic/Operational Plan with the Accounting Officer.
- Obtain Audit Committee approval for the changes made.

The strategic plan should be re-assessed on at least an annual basis and any changes incorporated into the operational plan for the following year.

Key steps:

1. Identify changes in objectives/risk factors.



- This should be achieved by ongoing dialogue with the departmental management and the Risk Advisory section of the Internal Audit Unit.
 - The Strategic/Operational Plan should also be reassessed where there are delays on current engagements.
2. Update risk register.
 - Performed by the Risk & Compliance
 3. Assess impact on plan.
 - This assessment should be performed by Manager Internal Audit.
 4. Revise Strategic/Operational Plans (at least annually) and follow previously determined review and approval processes.

➤ Planning – Reassess plan

Templates
N/A

3. Phase 2: Engagement Planning

3.1 Introduction

International Standards for the Professional Practice of Internal Auditing:

2200 – Engagement Planning

“Internal Auditors should develop and record a plan for each engagement, including the scope, objectives, timing and resource allocations.”

2201– Planning Considerations

“In planning the engagement, the internal auditors should consider:

The objectives of the activity being reviewed and the means by which the activity controls its performance.

The significant risks to the activity, its objectives, resources, and operations and the means by which the potential impact of risk is kept to an acceptable level.

The adequacy and effectiveness of the activity’s risk management and control systems compared to a relevant control framework or model.

The opportunities for making significant improvements to the activity’s risk management and control systems.

2201.A1 *“...internal auditors should establish a written understanding about objectives, scope, respective responsibilities and other expectations, including restrictions on distribution of the results of the engagement and access to engagement records”.*

2210 – Engagement Objectives

“Objectives should be established for each engagement”

2210.A1 *–“Internal Auditors should conduct a preliminary assessment of the risks relevant to the activity under review. Engagement objectives should reflect the results of this assessment”.*

2210.A2 *– “The internal audit should consider the probability of significant errors, irregularities, noncompliance, and other exposures when developing the engagement objectives”.*

Comprehensive, detailed engagement planning is critical to provide an effective, high quality audit. The engagement planning stage enables the internal audit team to gain an understanding of the engagement to be performed, and identify the risks and control objectives to develop the scope of the engagement. In addition, the internal



audit team can use the planning phase to obtain management buy-in to the approach, scope and timeframes.

3.2 Engagement Initiation

Overview:

All engagements should be initiated at the direction of the Audit Manager/ Internal Audit Specialist in accordance with the approved Strategic/Operational Plan.

Prior to initiating the engagement, the Internal Audit Manager should review the risks and other factors that have driven the inclusion of the specific engagement in the operational plan for the year to determine if there has been any significant changes in the department's operating conditions, which have resulted in the risks associated with the scheduled engagement changing and which may require that the engagement be expanded, delayed or cancelled. If this is the case, the operational plan for the year would need to be revised in accordance with the process set out under 2.7.

Key objectives:

- Create the linkage between Strategic/Operational plans and engagement plan.
- Develop a broad /general understanding of those entity processes included in the auditable area/engagement.
- Communicate timeframes and requirements to Head of Department and internal audit staff
- Obtain Management buy-in to approach, scope, timeframes

Key steps:

1. Set up the client file.
 - Each internal audit engagement is documented manually. A file should be created for each engagement.
2. Advise the Programme Manager of the audit to be conducted and arrange a date and time for the opening meeting.
 - This can be done telephonically by the Internal Audit Manager.
 - The opening meeting should be attended by the Head of Department, the Programme Manager and other client management, as relevant. The Programme Manager and Internal Auditor should facilitate the arrangement of a date with all relevant attendees.
3. Draft a Notification Letter to the Head of Department detailing the high level objectives and the preliminary scope of the audit and the team members.
 - The Notification Letter is designed to advise the Municipal Manager, Head of Department about the audit we intend conducting, to formally introduce the preliminary scope and primary objectives of the engagement, and to introduce the key members of the engagement team and to confirm the date and time of the opening meeting.
 - The agenda for the opening conference meeting should be attached as an addendum to the notification letter.
 - The Notification Letter should be sent out at least two weeks prior to the beginning of the engagement planning of any engagement.
 - The Notification Letter should be written and delivered by the Internal Auditor to the Head of Department. The Programme Manager of the area being audited should be copied on the Notification Letter.



- All Notification Letters should be sent to the Audit Manager for signature, prior to being distributed to the client, in line with delegated signing authority and protocol.
4. Obtain an understanding of the department and area under review.
 - An understanding of the operations of the business unit being audited is fundamental to effective engagement planning and efficient auditing. It is essential that sufficient information be obtained so that we can identify and understand the risks, processes and practices that may have an impact on the internal audit engagement, and provide meaningful advice and constructive suggestions.
 - The Internal Auditor should review the information obtained in phase 1 and should perform a more detailed review of the client's business and the process being reviewed. This typically will include:
 - reviewing the client's website;
 - making enquiries from the previous internal auditor;
 - reviewing previous internal and external audit reports;
 - reviewing descriptions of the information, accounting and control systems, including the prior year systems descriptions;
 - reviewing background information about the business units operations, goals and objectives;
 - obtaining the operational risk assessment results from Risk Advisory services; and
 - reviewing the organogram for the establishment.
 5. Conduct an opening meeting with the Head of Department to understand areas of concern and obtain information relevant to the auditable area/engagement.
 - The Manager: Internal Audit, Internal Auditor should attend the opening meeting.
 6. Prepare an Engagement Letter/Planning memorandum addressed to the Head of Department detailing the primary objectives and the final scope of the audit, as agreed in the opening meeting, as well as the engagement team members.
 - Based on the planning decisions made in the Strategic/Operational Plan, and further information obtained in the engagement initiation phase, the primary objectives and the scope of the engagement should be clearly defined.
 - The Engagement Letter/Planning memorandum is designed to communicate the final scope and primary objectives of the audit to the Head of Department, as well as to introduce the key members of the engagement team.
 - The Engagement Letter/Planning memorandum should be sent out within one week of the opening conference meeting.
 - The Engagement Letter/Planning memorandum should be written and delivered by the Internal Auditor to the Head of Department. The Programme Manager of the area being audited should be copied on the Engagement Letter/Planning Memorandum.
 - All Engagement Letters/Planning memorandum should be sent to the Audit Manager for signature, prior to being distributed to the client, in line with delegated signing authority and protocol.
 7. Summarise the key engagement planning decisions in the audit planning memorandum.
 - The audit planning memorandum should summarise the engagement initiation phase and provides a platform for the Manager: Internal Audit to review and ensure that the planning is progressing satisfactorily.
 - The results of the steps completed thus far should be documented in an audit planning memorandum. The audit planning memorandum typically includes the following:



- Engagement Title;
 - Engagement code;
 - Engagement Sponsor;
 - Background information;
 - Rationale for the audit (being key risks identified in the strategic planning phase, specific management concern, legislative requirement, follow-up review etc);
 - Engagement objectives and scope;
 - A high level overview of the process or business area, including control; objectives and risks;
 - Timeline of key events (e.g. opening meeting, commencement and completion of fieldwork, closing meeting, report issuance);
 - Audit team members and their roles;
 - Stakeholders i.e. intended recipients of the audit report;
 - Audit challenges and mitigating actions;
 - Work locations;
 - Time and expense budget.
- The Manager: Internal Audit, Head of Department should sign the audit planning memorandum prior to the commencement of fieldwork.
- Detailed planning – notification letter
 - Detailed planning – preliminary review
 - Detailed planning – opening meeting
 - Detailed planning – engagement letter/audit planning memorandum

Templates

- ✓ Notification Letter and agenda
- ✓ Opening Meeting minutes
- ✓ Engagement Letter/Audit planning memorandum

3.3 Engagement Risk Assessment and Scope

International Standards for the Professional Practice of Internal Auditing:

2220 – Engagement Scope

“The established scope should be sufficient to satisfy the objectives of the engagement”.

2220.A1 – *“The scope of the engagement should include consideration of relevant systems, records, personnel, and physical properties, including those under the control of third parties”.*

2210.A1 – *“Internal Auditors should conduct a preliminary assessment of the risks relevant to the activity under review. Engagement objectives should reflect the results of this assessment”.*

Overview:

The purpose of an engagement risk assessment at the auditable activity, process or system level is to determine the risk profile and strategy for the internal audit to be performed. Performing the engagement risk assessment during the engagement planning phase enables us to better focus our audit scope.

Determining the scope in this engagement planning stage is focused on the key risk areas so that we can outline what to cover during the execution phase. Developing test plans occurs after we understand the control activities in place to manage the risks identified.



Special consideration should be given to identification of fraud during the planning and scoping phase of each internal audit engagement. The engagement team should have sufficient knowledge to identify the indicators of fraud, and should call on specialised expertise where appropriate.

Key objectives:

Identify and evaluate detailed risks and applicable controls in the entity process.

Key steps:

1. Identify and document the control objectives in relation to the activity, process or system being reviewed.
2. Identify and document the risks that will impact the achievement of these control objectives and update the department risk profile
3. Document our understanding of the system/process flow.
 - The Supervisor should document the detailed system description and the walkthrough.
 - Our documentation should encompass the entire process of initiating, recording, processing and reporting individual transactions as this will enable us to make judgements as to which of the controls we need to evaluate.
 - This documentation should take the form of flowcharts or narratives.
 - The Internal Auditor should prepare these working papers.
 - The Audit Manager should review and approve these working papers.
 - The documented systems description should be reviewed and approved by the Programme/Process Manager.
 - The Programme/Process Manager should sign the systems description as evidence of approval.

Note: The original approved systems description should be kept in the hard copy engagement file.

4. Perform a walkthrough to validate our understanding of the system/process flow.
5. Identify controls that mitigate the risks identified and evaluate their design effectiveness.
6. Summarise the assessment in a risk and controls matrix.
 - The Internal Auditor should document the risk and control matrix.
 - The Audit Manager should review and approve these working papers.
7. Identify and document gaps in controls and/or recommendations for improvement for communication to the client.

Glossary of terms and further guidance on the COSO Framework

Control Objectives

We need to understand the control objectives in relation to the activity, process or system being audited. You can identify business and control objectives through interviews, research and professional judgement. Control objectives may be articulated in a variety of documents including the department mission statement, balanced scorecard initiatives, business plans and budgets.

Risks

The risks you need to identify directly relate to the control objectives in terms of the question "What can go wrong to prevent the achievement of the control objectives?". It is these risks which will ultimately drive the scope of our audit and will be reflected



in our engagement plan. Important considerations include risk circumstances and indicators.

Risk circumstances are factors or drivers that can lead to the occurrence of a problem or event relative to a specific risk (i.e.: answer the question "Could there be a problem?"). The more circumstances that exist, the more likely it is that there is a problem in a particular area. Risk indicators are events or existing situations that are evidence that a problem exists.

By identifying and considering the risk circumstances and indicators, the underlying causes of risk areas become more apparent.

Controls

The criteria for evaluating the adequacy of design of specific controls include:

- Whether the controls respond to a control objective.
- Whether the control is capable of effectively ensuring that a desirable outcome occurs (for example, whether it applies at the right frequency or level of precision).
- Whether management has implemented the control.

Utilising the COSO Framework when Evaluating Controls

To facilitate the evaluation of internal controls the COSO framework should be adopted. The relationship between objectives, risk and controls is outlined below:

Objectives

- **Completeness**
 - What ensures that all recorded transactions are accepted by the system (once and only once)?
 - What prevents duplicate posting by the system?
 - What detects any transactions that are rejected and what ensures these are addressed and fixed?
- **Accuracy**
 - What ensures that key data elements for transactions (including standing data) recorded and input to the computer are reasonably correct?
 - What ensures that changes to standing data are accurately input?
- **Validity**
 - What prevents unauthorised transactions, including changes to standing data?
 - What ensures transactions, including standing data, are not fictitious and they relate to the business?
- **Restricted Access**
 - What prevents or detects unauthorised amendments of data?
 - What ensures confidentiality of data?
 - What ensures that assets are physically and logically protected from theft and misuse?
 - What prevents the same individual from doing incompatible transactions such as initiating a purchase order, gaining access to check runs and updating the accounts payable detail?

Control objectives should also be established for operating and compliance elements of COSO.



When evaluating effectiveness of internal controls a number of factors have to be considered as follows:

- Alignment between the controls and the risks identified – Our evaluation will focus on whether the controls appear to be effective in achieving management's stated objectives and managing the related risks.
- Nature of the control – For example, a high level business performance review rarely provides sufficient assurance to be considered an effective control, but properly designed detailed information processing controls should provide sufficient assurance.
- Follow-up actions taken by the organisation - For a control to be effective there needs to be adequate follow-up of issues and exceptions, in a timely manner.
- Frequency of control – This will affect whether the control will detect or prevent the risk identified on a timely basis. In some cases, a detective control may be adequate, but in other cases, the entity should ensure there are adequate preventative controls.
- Period covered by the control – For audit purposes, we may need to obtain evidence that a control is effective for a reporting or specified period.

We evaluate controls generally combining our evaluation of all the evidence available to us from our internal audit work.

Other Considerations:

When evaluating internal controls in relation to the control objectives, we should also consider the concepts of economy and efficiency by evaluating the controls over quantity, quality, time and cost. For example:

- Quality – of input, output, resources and performance.
 - Quantity – of input, output, resources, and desired results.
 - Time – deadlines.
 - Cost – in relation to quality, quantity and time.
- Detailed planning – engagement risk assessment and scope
- Templates**
- ✓ Risk and control matrix
 - ✓ Systems documentation
 - ✓ Walkthrough testing

3.4 Engagement Resource Allocation

International Standards for the Professional Practice of Internal Auditing:

2230 – Engagement Resource Allocation

"Internal auditors should determine appropriate resources to achieve engagement objectives. Staffing should be based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources".

Key objectives:

- To allocate appropriately skilled and experienced staff to the engagement that will result in the achievement of the engagement objectives.

Key steps:

1. Determine the staff required for the engagement, taking into account the complexity of the assignment and the need for specialist skills.

Detailed planning – resource allocation



Templates

- ✓ Engagement costing template

3.5 Engagement Project Plan and Audit Programme

International Standards for the Professional Practice of Internal Auditing:

2240 – Engagement Work Program

"Internal Auditors should develop work programs that achieve the engagement objectives. These work programs should be recorded."

2240.A1 – *Work programs should establish the procedures for identifying, analyzing, evaluating, and recording information during the engagement. The work program should be approved prior to its implementation, and any adjustments approved promptly."*

Key objectives:

Develop the engagement approach (scope of work, method of testing, depth of testing etc.)

Key steps:

1. Develop the audit programme for the auditable area/engagement.
 - A testing strategy should be prepared based on the evaluation of controls. The testing strategy should be formulated into a testing plan. The testing plan documents the linkage between the identified risks and controls (as documented in the risks and control matrix) to the associated tests. A well-constructed testing plan is essential to completing the audit in an efficient manner, by providing the following:
 - A systematic plan for each phase of the work that can be communicated to all internal audit personnel.
 - A means of directing the internal audit staff assigned.
 - A means by which the Internal Auditor can review and compare performance with approved testing plans.
 - The basis for a summary record of work performed.
 - Assistance in familiarising successive audit staff with the nature of work previously carried out.
 - The further information on types of testing as set out in the further guidance under 4.3 should be considered in developing the audit programme.
 - The audit programme should be developed by the Internal Auditor based on the key controls identified in risk and control matrix.
 - The audit programme should be reviewed by the Internal Audit Manager.
2. Develop a detailed engagement project plan setting out the tasks to be completed.
 - The detailed engagement project plan should be prepared by the Internal Audit Manager.
 - Staff members should be allocated to the specific tests depending on their level of competence and experience.
 - Hours should be allocated to the specific tests and the timing and specific milestones/deadlines documented.
 - Adequate provision should be made in the detailed engagement project plan for on-site supervision and review.



- Throughout the engagement, the Internal Auditor should monitor the execution of the engagement project plan and prepare weekly updates, using the status report template, for the Internal Audit Manager.
- Every two weeks, the relevant line managers should be informed of the progress of the internal audit engagement.

Note:

1. The status of the engagement should be tracked, by the Audit Manager on TeaMMate.
 - Detailed planning – detailed engagement project plan
 - Detailed planning – audit programme

Templates

- ✓ Detailed engagement project plan
- ✓ Audit programme
- ✓ Status report
- ✓ Progress report to line management

3.6 Engagement Project Plan and Audit Programme Approval

International Standards for the Professional Practice of Internal Auditing:

2240.A1 – Approval of Work Programs

“Work programs should establish the procedures for identifying, analyzing, evaluating, and recording information during the engagement. The work program should be approved prior to its implementation, and any adjustments approved promptly”.

Key steps:

1. Review and approve the audit programmes and engagement project plan.
 - The Internal Audit Manager should review and sign the engagement project plan and audit programmes preferably prior to the commencement of fieldwork but not more than one week after the commencement of fieldwork.

Detailed planning – engagement project plan and audit programme approval

Templates

N/A

4. Phase 3: Performing the Engagement

4.1 Introduction

International Standards for the Professional Practice of Internal Auditing:

2300 – Performing the Engagement

“Internal Auditors should identify, analyze, evaluate, and record sufficient information to achieve the engagement’s objectives”.

The overall objective is to ensure that the internal audit team, having the knowledge of the processes undertaken in phase 1 and 2, execute the internal audit work



planned in a structured and systematic manner, delivering work of a high quality, in order to achieve the objectives set for the engagement.

Once the engagement planning is complete, the engagement team will execute the audit programme. This phase includes the controls testing, potential substantive testing and formulation of findings. The audit programme will be re-evaluated throughout the different steps of the execution phase to address any new information obtained.

4.2 Mobilising the Engagement Team

Key objectives:

- Communicate the schedule of work and other engagement requirements to the internal audit team.
- Establish execution and work paper documentation protocols.

Key Steps:

1. Conduct a team kick-off meeting.
 - The objective of the team kick-off meeting is to communicate the approach to the audit and to promote a cohesive internal audit team.
 - The team kick off meeting should be facilitated by the Internal Audit Manager
 - All members of the internal audit team, up to the Audit Manager, should attend.
 - Kick-off meeting activities should include discussion and agreement on the content of:
 - The approved APM;
 - The approved engagement project plan and work programme;
 - Documentation and review practices (refer to 4.5 for further guidance on planning for an effective review process);
 - Development objectives for each team member.

Execution – Team mobilisation

Templates

N/A

4.3 Execution of the Audit Programme

International Standards for the Professional Practice of Internal Auditing:

2310 – Identifying Information

“Internal Auditors should identify sufficient, reliable, relevant, and useful information to achieve the engagement’s objectives”.

2320 – Analysis and Evaluation

“Internal Auditors should base conclusions and engagement results on appropriate analyses and evaluations”

Key objectives:

- Perform the approved control testing.
- Develop the basis for audit findings and recommendations.



Key steps:

1. Perform controls testing in accordance with the approved audit programme.
 - At the Engagement Risk Assessment and Scope phase, the controls would have been assessed to determine whether they had been appropriately designed (refer to 3.4). The audit programme would have been prepared to enable testing which should enable the internal audit team to determine whether the control is working as it was designed to.
 - In executing the audit programme, information that is sufficient, competent, relevant, and useful to provide a sound basis for audit observations and recommendations should be collected.
 - Sufficient information is factual, adequate, and convincing so that a prudent, informed person would reach the same conclusions as the internal auditor.
 - Competent information is reliable.
 - Relevant information supports audit observations and recommendations and is consistent with the objectives for the engagement.
 - Useful information helps the department meet its goals
2. Perform substantive testing in accordance with the approved audit programme.
 - Once a control deficiency is identified, the need to perform substantive testing to assess the potential impact of control deficiencies, should be determined in discussion with the Internal Audit Manager.
 - The additional substantive tests should be developed by the Internal Auditor and should be approved by the Internal Audit Manager, prior to the substantive testing commencing.
 - In consultation with the Manager: Internal Audit, the Internal Auditor should determine whether reporting to Forensic Investigations is required.
3. Identify all potential findings from the work performed and formulate recommendations.
 - The Internal Auditor should document all findings identified during the audit.
 - All documentation should be reviewed by the Internal Audit Manager during the audit to ensure that all findings have been identified and documented.
 - The conclusions on all areas of audit work performed should be reviewed to ensure that the conclusions made are appropriate in light of the findings and to identify potential additional findings for inclusion in the audit report. These might include:
 - Control environment findings;
 - Design effectiveness findings ;
 - Operating effectiveness findings;
 - Substantive testing findings.
 - Sufficient details of the control deficiency should be provided to enable the reader of the report to draw conclusions on the extent of the control deficiency. For example, the number of errors in the sample and rand values.
4. Rank each potential audit finding.
 - The potential audit findings should be ranked according to the severity of the given risk exposure taking into account the probability of occurrence and the significance of the impact.
 - In determining the ranking of the audit findings, the potential effect of compensating and mitigating controls should be considered.
 - The following rating matrix has been adopted to rate internal audit findings:



Rating	Description
High	Key exposure identified has a potential for major impact on the Municipality and should be resolved within three months.
Medium	Exposure identified is unlikely to have a major impact on the Municipality, but should be resolved within six months.
Low	Exposure identified does not have a major impact on the Municipality, but should be resolved in due course.

5. Discuss potential findings with relevant municipal staff member and obtain initial comments on the remediation action that will be taken.
 - The potential audit finding should be discussed with relevant departmental staff member to agree the factual accuracy of the finding, including the potential impact, and the resultant risk exposure and to obtain preliminary comments on the remedial action that will be taken.

Note: Although identified as a separate step, the formulation of findings is performed throughout the engagement planning and execution phases of the audit.

6. Re-evaluate the scope.
 - Throughout the execution phase, the scope should be constantly re-evaluated in light of testing results and the identification of risks previously not known. The internal audit team should review and adjust the audit programme as a result of control weaknesses not identified in the planning process or significant errors that affect the scope of work.
 - Any such changes should be appropriately documented and potential changes to the engagement timeline should be assessed.
 - Execution
 - Exceptions

Templates

- ✓ Working paper format
- ✓ Exception format

Further guidance on developing audit programmes and testing controls

Determine Key Controls for Testing

The nature and scope of testing to be performed is based on the auditor's judgement of the probability and impact of the risks associated with the control and this should drive the nature and level of testing to be performed.

Controls may be preventative or detective in nature. A detective control (e.g.: reconciliation) which operates downstream from a preventative control (e.g.: edit check) should be tested separately from the preventative control as the successful performance of the detective control would not provide direct evidence as to the effectiveness of the edit check as a control in its own right.

Determine Test Objectives and Control Attributes to be Tested



Tests of controls are designed to obtain evidence to verify the operating effectiveness and design of controls. Operating effectiveness means that the controls are being applied as designed on a sufficiently consistent basis.

The test objective should identify the control and state the attributes to be evaluated, as follows:

- Was the control executed correctly with respect to the control objective?
- Did the right person perform the control?
- Was the control performed consistently during the period under examination?

Determine the Time Period over which Control Testing will be performed

When determining the period over which control testing will be performed, the following should be considered:

- Periods when controls may not be operating effectively, such as during vacation periods of key personnel or periods of high personnel turnover, significant changes in management or systems conversion.
- Change of controls during the period under audit.
- New systems.

Testing types

There are four basic testing techniques (inquiry, observation, examination of evidence and re-performance) which should be used to obtain our audit evidence.

Inquiry

Direct inquiry – Inquiry consists of seeking information of knowledgeable persons inside or outside the entity. Evaluating responses to inquiries is an integral part of the inquiry process. Inquiry involves:

- Considering the knowledge, objectivity, experience, responsibility and qualifications of the individual to be interviewed.
- Asking clear and concise questions to understand how a control has been applied (e.g.: when, how often, with what data).
- Identifying whether the individual has understood the appropriate objectives of a control procedure (e.g.: by asking about typical or expected errors, follow-up protocols and transactions that do not follow the normal procedure).
- Using open-ended or closed-ended questions appropriately.
- Listening actively and effectively.
- Considering the interviewee's responses and asking follow-up questions.

Inquiry alone ordinarily will not provide sufficient audit evidence to detect the presence of a control or to support a conclusion about the operating effectiveness of specified controls. Ordinarily, tests in addition to the use of inquiry should be performed to obtain sufficient appropriate audit evidence.

Inquiry is usually required when seeking to understand whether a manual control that involves judgement has been properly applied. For example, inquiry of a member of management who approves reconciliations or transactions can help determine whether the individual understands what should be identified for follow-up and whether the approval process has been done diligently.

Analytical procedures – Analytical procedures consist of evaluations of financial information made by a study of plausible relationships among both financial and non-financial data. Analytical procedures also encompass the investigation of identified



fluctuations and relationships that are consistent with other relevant information or deviate significantly from predicted amounts. It is important to note that effective use of analytical procedures requires the development of an independent expectation of the relationships expected to exist prior to executing the procedures based on the knowledge of the business, industry, trends or other accounts.

Observation

Observation consists of looking at a process or procedure being performed by others. Examples include observation of the cycle counting of inventories by the entity's personnel or observation of the performance of control procedures that leave no audit trail. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place and by the fact that the act of being observed may affect how the process or procedures is performed.

Examination of documents

Inspection of information of data – Inspection consists of examining records or documents whether in paper form, electronic form, or other media. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.

Re-Performance

Recalculation – Recalculation consists of checking the arithmetical accuracy of documents or records.

Re-performance – Re-performance is the independent execution of procedures or controls that were originally performed as part of the entity's internal control, either manually or through the use of CAAT, for example, re-performing the bank reconciliation.

Determine which Control Testing Technique should be used

When testing internal controls, the objective is to obtain sufficient assurance to offer valid findings and recommendations on the design and/or operation of controls, based on the agreed scope set out on advance

A combination of techniques may be used in order to test the controls. While techniques to use depend on many factors, but primarily should be based on:

- The nature of the control, in particular the degree of susceptibility to change. A control that is susceptible to change usually should not be observed as the observation may not be representative of the operation of the control under normal circumstances.
- The frequency and extent of the control. A control that operates infrequently and requires a significant effort, such as a physical count of inventory, should not be re-performed because of the impracticality of doing so but may be observed.
- The likelihood of control weakness, based on the assessment of the design of the control. For example, we may conclude that a control is highly unpredictable



based on its manual nature, past failures or complexity of process. In this case, we may prefer re-performance to capture the variations in the process.

- Significance of the control to the control environment and how much reliance is being placed on it. For example, we may decide to test a compensating control more rigorously if the principal control has already been found to be ineffective.

Sampling

Sampling is the application of auditing procedures to a representative group of less than 100% of the items within a homogenous population for the purpose of evaluating the population.

Sampling approaches can either be statistical or non-statistical in nature. Both are commonly used and have particular advantages and disadvantages. The most commonly used sampling approach is non-statistical sampling. The sampling guidance detailed below, while directed to non-statistical sampling, is grounded in statistical theory and is designed to provide the necessary information to determine appropriate sample sizes and selection techniques, and properly project and evaluate results from non-statistical sampling.

Non-statistical sampling

There are three key steps in a non-statistical sampling process:

- Determine the control test objective, population and sampling unit;
- Determine the sample size;
- Select the sample for testing.

Determine the sample size

a) Sample sizes for testing manual controls

The sample size will depend on the frequency of the control being tested and the level of evidence that is judged to be necessary by the internal audit team.

The following is a guideline in determining the minimum sample sizes:

Frequency of Control	Sample Size
Annual	1
Quarterly	2
Monthly	2 (minimum) to 5 (maximum)
Weekly	5 to 15. Select 10 if you require a mid-range
Daily	20 to 40. Select 30 if you require a mid-range
Multiple times per day	25 to 60. Select 30 or 45 if you require a mid-range

Sampling is a judgemental decision to be made by the engagement team and client. The following factors may be indicative that a relatively larger sample size should be considered:

- The greater the potential financial loss or adverse event to the organisation if the control is not effective or fails;
- The more complex the control;
- The more significance of judgement in control operation.



b) Sample sizes for testing of automated controls

The testing of manual controls is generally more extensive than that of testing automated controls. In some instances, provided that general computer controls have been tested and are deemed to be effective, the testing of a single operation of an automated control may be sufficient to validate its effective operation.

Select a sample

The objective for any sample selection method is to obtain a representative sample of the population. To increase the likelihood that a sample will be representative, all items in the population should have an equal opportunity of being selected. Common methods of selecting a sample, using non-statistical sampling approach, are as follows:

a) Random selection

- A method that ensures that all items in a population have an equal chance of being selected.
- Involves no human judgement, and is therefore a preferable selection technique as it excludes bias.
- Random number software can be used to select the sample.

b) Systematic selection

- A systematic method for selecting a representative sample, where the use of random number selection is not deemed efficient (e.g.: time constraints, population data is not readily available in an electronic format).
- A systematic approach is used by the auditor to select items, to minimize any potential human judgement or bias. Every nth item within the population is selected in accordance with a defined sampling interval.
- The sampling interval is established based on the number of items within the population, without reference to size or monetary value of the item.

Systematic sampling is not appropriate when the items in a population are not randomly ordered.

c) Haphazard selection

A method for selecting a representative sample size using human judgement. The auditor, without any conscious bias, selects sample items randomly, i.e. without any special reason for including or omitting items from the sample. This may be an acceptable alternative to random selection when electronic data is not readily available and if the team is confident selection conditions will not induce bias.

Further guidance on assessing the actual or potential impact of internal audit findings

In assessing the actual or potential impact of internal audit findings, the following factors should be considered:



Business Risk: *The threat that an event or action will adversely affect the municipality's ability to achieve its objectives and to execute its strategies successfully.*

Strategic Risks: *Are risks that relate to doing the wrong thing. For example, taking on a business activity that results in the emission of pollutants above legally acceptable levels.*

- Are the critical strategies appropriate to enable the department to meet its business objectives?
- What are the risks inherent in those strategies, and how might the department identify, quantify, and manage these risks?
- How much risk is the department willing to take?
- What risks result from e-business developments?

Operational Risks: *Are risks that relate to doing the right things the wrong way. For example, asking employees to practice risk management practices without providing training to the employees.*

- What are the risks inherent in the processes that have been chosen to implement the strategies?
- How does the department identify, quantify, and manage these risks given its appetite for risk? How does it adapt its activities as strategies and processes change?

Financial Risks: *Are risks that relate to losing financial resources or incurring unacceptable liabilities. For example borrowing money at a rate of interest that fluctuates based on the prime rate of interest.*

- Have operating processes put financial resources at undue risk?
- Has the department incurred unreasonable liabilities to support operating processes?
- Has the department succeeded in meeting measurable business objectives?

Information Risks: *Are the risks that relate to the access to or use of inaccurate, irrelevant or untimely information; unreliable systems and inaccurate or misleading reporting in support of decisions. For example the ability to forecast future costs based on historical trends.*

- Is our data/information/knowledge reliable, relevant, and timely?
- Are our information systems reliable?
- Do our security systems reflect our e-business strategy?

Environmental Risks: *Are usually determined by sources outside of the control of the department. They are also sometimes referred to as "external risks" facing a department. For example the possible occurrence of a natural disaster and its impact on a department's operations.*

Regulatory Risks: *Are usually determined by government. They are also sometimes referred to as "external risks" facing a department. For example non-compliance with labour legislation.*



The impact on the Department's image: *Negative corporate image/goodwill of the organization in the business environment as a result of particular effect of risk materializing.*

The impact on the third parties: *Stakeholders' negative perceptions about the department as a result of the risk materializing.*

The impact on employee morale: *Negative employee behaviour as a result of a particular risk materialising.*

In addition, when evaluating findings, the underlying cause of the finding should be determined, as follows:

Strategic Management	Override, lack of direction and role clarity, delegation of authority
Systems/Internal Control	Appropriateness, non-compliance
Operational Management	Supervision, override, role clarity
Staffing	Training, turnover, workload, development, mix, skills

4.4 Documentation of Audit Work

International Standards for the Professional Practice of Internal Auditing:
2330 – Recording Information

"Internal Auditors should record relevant information to support the conclusions and engagement results."

Overview:

Working papers are prepared to record the information obtained and the analyses made in planning and conducting an internal audit. Proper audit documentation is critical to an effective, high quality audit and a complete set of working papers should be retained for each engagement.

The overall objective is to ensure that sufficient documentation exists to enable the supervision and review of the work and to provide support for the internal audit team's findings.

Key objectives:

- Assist in the planning, performance and supervision of the audit.
- Provide a basis for the review of the quality of the work.
- Provide the support for the internal audit findings and recommendations.
- Provide evidence that audit standards have been followed.
- Provide the basis for evaluating the performance of the members of the internal audit team.

Key steps:

1. Document the work performed in the appropriate folder and step in the TeamMate file, using the templates provided.
 - The team member performing the internal audit work should prepare audit documentation in sufficient detail to provide a clear understanding of its purpose, source and the conclusions reached.
 - Documentation should include:
 - Source and basis of selection of the sample;



- The nature and extent of procedures performed;
- The timing of the procedures performed;
- The audit evidence obtained;
- The results of the testing;
- The conclusions reached;
- The documentation should provide a clear link to any findings arising or issues.

Note: Although included as a separate step under execution, appropriate audit documentation should be prepared for all phases of the internal audit process as set out in this methodology.

4.5 Supervision and Review

International Standards for the Professional Practice of Internal Auditing:

2340 – Engagement Supervision

“Engagements should be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.”

Overview:

All work should be reviewed to determine whether it was adequately performed and to evaluate whether the results are consistent with the findings and recommendations included in the report.

The overall objective is to ensure a quality deliverable at minimum “cost”.

Key objectives:

- Provide ongoing direction and supervision to team members throughout the assignment.
- Ensure adequate documentation of the work performed.

Key steps:

1. Plan for an effective review process.
 - Common working practices for documentation, review, coaching notes etc. should be agreed at the kick off meeting,
 - The persons that will be responsible for performing the work and performing the review, as well as the relevant timing of the review, should be agreed at the kick off meeting,
 - Team members should be properly briefed on their particular areas immediately after the team kick off meeting.
 - Team members should be provided with effective coaching throughout the assignment to help ensure that the work performed is appropriate.
2. Conduct reviews as appropriate.
 - Reviews should be performed regularly, while the engagement is in progress.
 - The review should be performed in an interview format and should be performed on site.
 - For those questions that cannot be resolved in the interview, coaching notes should be raised by the team member responsible for the area, at the direction of the reviewer.
 - Coaching notes should be answered promptly by the team member.



- The reviewer should clear the coaching notes promptly.
- A final review of the work completed should be performed to ensure that all coaching notes have been cleared.

Note: Although included as a separate step under execution, supervision and review is an ongoing process throughout the audit

5. Phase 4 : Communicating Results and Completion

5.1 Introduction

International Standards for the Professional Practice of Internal Auditing:

2400 – Communicating Results

"Internal auditors should communicate the engagement results"

2410 – Criteria for Communicating

"Communications should include the engagement's objectives and scope as well as applicable conclusions, recommendations and action plans".

2420 – Quality of Communications

"Communications should be accurate, objective, clear, concise, constructive, complete, and timely."

2500 – Monitoring Progress

"The chief audit executive should establish and maintain a system to monitor the disposition of results communicated to management."

2600 – Resolution of Management's Acceptance of Risks

"When the chief audit executive believes that senior management has accepted a level of residual risk that may be unacceptable to the organization, the chief audit executive should discuss the matter with senior management. If the decision regarding residual risk is not resolved, the chief audit executive and senior management should report the matter to the board for resolution."

Effective communication of the results of an internal audit engagement is critical to the success of the Internal Audit Unit. The internal audit report is the only public record of the work performed and becomes the most visible measure by which the Internal Audit Unit is rated.

The overall objective of the communication process is to ensure that the results of the internal audit engagement are communicated to management and the Audit Committee in a manner that is accurate, clear, concise and timely. Internal audit reports also provide a record to facilitate the subsequent follow-up of the actions taken by management in addressing risks identified.

5.2 Reporting to Senior Management

5.2.1 Draft reporting

Key objectives:

- Develop the draft Internal Audit Report incorporating the scope of the engagement and the findings and recommendations arising from the work performed.
- Facilitate final auditee agreement as to facts included in the report.



- Obtain management input as to action plans and timing thereof.

Key steps:

1. Prepare the draft Internal Audit Report.

- The draft Internal Audit Report should include the following:
 - Introduction and background;
 - Audit objectives and scope;
 - Audit approach;
 - Value added statement;
 - Limitations on scope and exclusions;
 - A paragraph on fraud and internal control;
 - Audit Conclusion;
 - Detailed findings and recommendations and risk ratings.
- In preparing the audit conclusion on the effectiveness of the controls in the process/area being reviewed, the following matrix should be used:

Rating	Description
Catastrophic	A catastrophic level of residual risk exposure due to extreme inefficient and ineffective operation of controls which needs excessive effort and urgent attention for improvement
High	A high level of residual risk exposure due to inefficient and ineffective operation of controls which needs major effort and urgent attention for improvement
Medium	A medium level of residual risk exposure due to satisfactory controls to provide management with reasonable assurance that risks will not materialize but there is a room for improvement.
Low	A low level of residual risk exposure due to effective and efficient operation of controls which provides management with reasonable assurance that risks will not materialize and that the process objectives will be achieved
Insignificant	An insignificant level of risk exposure due to extremely effective and efficient controls which provide management with reasonable assurance that risks will not materialize and that the process objectives will be achieved

- The draft Internal Audit Report should be prepared by the Internal Auditor.
- 2. Perform an internal review of the draft Internal Audit Report.**
- The Audit Manager should perform the review of the draft Internal Audit Report.
 - All queries arising from the reviews should be resolved promptly.
- 3. Submit the final draft Internal Audit Report to the auditee.**
- The final draft Internal Audit Report should be clearly marked "DRAFT – FOR DISCUSSION PURPOSES ONLY".
 - A covering letter, addressed to the Head of Department, should be prepared by the Audit Manager. The letter should include:
 - Acknowledgment for the assistance granted to the Internal Audit Team;
 - A request for a close out meeting to discuss the preliminary findings contained on the final draft Internal Audit Report;



- The dates by which comments need to be provided (usually two weeks from the date of the close out meeting);
 - A target date for issuing the final Internal Audit Report.
 - The covering letter and the final draft Internal Audit Report should be signed by the Internal Audit Manager.
 - Two copies of the final draft Internal Audit Report should be delivered to the Auditee for review and comments.
 - The office copy of the final draft Internal Audit Report should be signed by the Auditee as evidence of receiving the draft report and should be returned to the Ubuhlebezwe Internal Audit Activity for filing.
4. Conduct a close out meeting with management and obtain management's responses.
- The Internal Audit Manager and the Internal Auditor in charge should conduct a close out meeting with the Programme Manager to discuss the findings, recommendations and preliminary management comments included in the final draft Internal Audit Report.
 - The Chief Director should also be invited to attend the close out meeting.
 - Any adjustments to the preliminary management comments as detailed on the final draft Internal Audit Report should be returned by the auditee, either by fax or e-mail, on a formal letterhead, within the timeframe agreed at the close out meeting (this is usually two weeks).
 - If comments are not received within this agreed timeframe, a letter should be sent informing the Head of Department that a further week is provided for submission of comments, after which the report will be finalised with no management comments.
 - The Internal Audit Manager should follow-up on outstanding and/or inadequate management comments promptly.
 - The Internal Auditor should update the final draft Internal Audit Report, and the exceptions in file, with the final management comments.
5. Perform the final review of the final draft Internal Audit Report (incorporating management's comments).
- The Internal Audit Manager should perform a final review of the final draft Internal Audit Report incorporating management's comments. Consideration should be given to the following when reviewing management's comments:
 - Management should provide an action plan, including the timeframe and who will be responsible for the action, for each finding to be reported.
 - Management's action plan should be reviewed to determine that it adequately addresses the finding, that internal audit's recommendation has been accepted and will be implemented or, an appropriate alternative recommendation has been proposed.
 - If management has already addressed the finding prior to the issue of the internal audit report, the finding must still be reported. In these instances it should be clear from the management comment that action was taken as a result of the internal audit work performed, so as to not lose the impact of the work performed.
 - If, despite further discussions with the auditee, agreement as to the recommendations made and an adequate action plan is not provided by management, a paragraph should be added to the final Internal Audit Report to indicate why the management's response to the findings is considered to be inadequate.



- If management has decided to accept the residual risk, knowing the risk rating assigned to the finding, management's decision should still be reported.
- If management has not provided comments with the timeframes agreed (i.e. after the second reminder), the report should be finalised without management comments. The cover letter to the report should detail the dates the report was issued and the dates of follow up correspondence.

Notes:

1. The status of the draft Internal Audit Report should be tracked using the "Internal Audit Report Tracker" document.
2. The office copy (hard copy) of the signed draft Internal Audit Report should be filed in the working paper file by the Internal Auditor in charge.
3. An electronic copy of the final draft Internal Audit Report should be filed on the Documents library by the Internal Auditor in charge.

➤ Draft Internal Audit Report

Templates

- ✓ Covering letter for final draft Internal Audit Report
- ✓ Draft Internal Audit Report
- ✓ Internal Audit Report tracker document
- ✓ Reminder for outstanding management comments

5.2.2 Final reporting

International Standards for the Professional Practice of Internal Auditing:

2440 – Disseminating Results

"The Chief audit executive should communicate results to the appropriate parties"

2440.A1- *"The chief audit executive is responsible for communicating the final results to parties who can ensure that the results are given due consideration."*

Key objectives:

- To communicate the final results of the internal audit incorporating specific management actions.

Key steps:

1. Prepare the final Internal Audit Report.
 - The final Internal Audit Report should be prepared by the Internal Audit Manager.
2. Perform an internal review of final Internal Audit Report.
 - The Internal Auditor should go through the final Internal Audit Report to ensure that all the relevant information is captured correctly.
 - The Manager Internal Audit should review and sign the final Internal Audit Report.
 - All queries arising from these reviews should be resolved promptly, prior to the report signing.
 - All steps in the working paper file should be signed off by the Audit Manager and all outstanding coaching notes cleared, prior to the final Internal Audit Report being issued.
3. Distribute the final Internal Audit Report in accordance with Auditee requirements.



- A covering letter, addressed to the Head of Department should be prepared by the Internal Audit Manager.
- The requisite number of copies of the final Internal Audit Report should be hand delivered to the auditee.
- The office copy should be signed by the Auditee as evidence of receiving the final Internal Audit Report and should be returned to the Ubuhlebezwe Internal Audit Activity.

Notes:

1. The status of the final Internal Audit Report should be tracked using the "Internal Audit Report Tracker" document. This is used to track the review process from the draft report stage to enable the Internal Audit Manager to easily determine the status of a report at a point in time.
2. The office copy (hard copy) of the final Internal Audit Report should be filed in the library by the Internal Audit Manager.
3. An electronic copy should be filed on documents library by the Internal Audit Manager.

➤ **Final Internal Audit Report**

Templates

- ✓ Covering letter
- ✓ Final Internal Audit Report
- ✓ Internal Audit Report tracker document

5.3 Reporting to the Audit Committee

International Standards for the Professional Practice of Internal Auditing:

2060 – Reporting to Board and Senior Management

"The chief audit executive should report periodically to the board and senior management on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan. Reporting should also include significant risk exposures and control issues, corporate governance issues, and other matters needed or requested by the board and senior management."

Overview:

The overall objective is to provide a snapshot of the internal audit activities and the significant findings, such that the Audit Committee has a reasonable understanding of the work performed and the related findings, such that they are able to provide the necessary oversight of the Internal Audit Activity.

Key objectives:

- Keep the Audit Committee informed of progress being made against the Strategic and Operational Plans.
- Highlight significant trends to senior management and the Audit Committee.
- Highlight significant findings arising from internal audit work performed, including management's plans to address those findings.
- Keep the Audit Committee informed as to the status of previously reported issues.
- Communicate changes to the Strategic and Operational Plans due to emerging risks, changes in scope and resource limitations.



Key steps:

1. Draft the Audit Committee Report.
 - The Audit Committee Report should be prepared by the Audit Manager.
 - The Audit Manager should prepare the Audit Committee Report in accordance with the format agreed in the Municipality's Strategic Planning phase (i.e. phase 1).
 - Strategic/Operational plans and Final Internal Audit Reports arising from phase 1, 2 and 3 should be used in the preparation of the Audit Committee Report.
2. Perform a review of the Audit Committee report.
 - The Internal Audit Manager should perform a review and sign the Audit Committee report.
3. Present the Audit Committee report to the Audit Committee.
 - The audit committee pack should be delivered to the Audit Committee members 5 days prior to the Audit Committee meeting.
 - The Internal Audit Manager, should present the Audit Committee report to the Audit Committee.

Notes:

- The office copy (hard copy) of the Audit Committee Report should be filed in the working paper file by the Internal Auditor in charge.
- The final electronic copy of the Audit Committee Report should be saved on documents library.

Templates

Audit Committee Report

5.4 Completion

Overview:

The overall objectives are to ensure that the engagement files adequately support the findings reported and that internal audit's performance is assessed to capture any process improvement opportunities and, in so doing, improve the level of service to the Municipality and enhance the skills of the Internal Audit Activity.

Key objectives:

- Complete the engagement in an orderly manner in accordance with professional obligations and engagement objectives.
- Evaluate performance (from auditee, staff development and engagement management perspectives).

Key steps:

1. Ensure all internal audit work is properly documented on the steps in the TeamMate file.
 - All internal audit work (planning, fieldwork and reporting) should be documented in the TeamMate engagement file.
 - All signed hard copy evidence should be scanned and attached in the TeamMate engagement file (e.g. signed receipt of draft/ final audit report).
 - At the completion of Phase 3, Performing the audit, all steps should be marked as complete by the preparer and reviewed by the reviewer and all coaching notes should be resolved and cleared in the file.



- At the completion of Phase 4. Reporting to senior management, all findings in the final report should be cross-referenced to the exceptions on the TeamMate engagement file to ensure that all reportable items have actually been reported to management.
 - The TeamMate file should be changed to "Read Only" by the Internal Audit Manager
2. Hold a team debriefing meeting.
 - A team debriefing meeting should be held to provide feedback on the results on the internal audit engagement and any issues arising, as well as to generate ideas for the continuous improvement of the internal audit process.
 3. Complete the Audit Completion Summary.
 - The purpose of the Audit Completion Summary is to ensure that all critical (and standard) steps in the internal audit process have been adequately performed and documented on the file.
 - The Audit Completion Summary should be prepared by the Internal Auditor and should be signed off by the Internal Audit Manager.
 4. Complete individual Team Member performance evaluations

➤ **Completion**

Templates

- ✓ Audit Completion Summary
- ✓ Team Debriefing Meeting Agenda

6. Phase 5 : Monitoring Process

6.1 Quality Assurance Programme

International Standards for the Professional Practice of Internal Auditing:

1310 – Quality Program Assessments

"The internal audit activity should adopt a process to monitor and assess the overall effectiveness of the quality program. The process should include both internal and external assessments."

1311 – Internal Assessments

"Internal assessments should include:

*Ongoing reviews of the performance of the internal audit activity; and
Periodic reviews performed through self-assessment or by other persons within the organization with knowledge of internal auditing practices and the Standards".*

1312 – External Assessments

"External assessments, such as quality assurance reviews, should be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization..."

Overview:

The overall objective is to ensure the quality of the Internal Audit Activity.

Key objectives:

- Ensure compliance with Ubuhlebezwe Internal Audit Unit Methodology and related policies.
- Facilitate consistent, quality service delivery.



Key steps:

1. Prepare a Client Satisfaction survey for completion by the auditee.
 - The Internal Audit Manager should prepare the client satisfaction survey.
 - The Internal Audit Manager should send a covering letter, addressed to the Head of Department, with the client satisfaction survey, requesting the auditee to complete the survey.
 - The Client Satisfaction survey should be sent together with the final internal audit report.
 - The Internal Auditor should follow-up on any outstanding client satisfaction surveys.
 - The Manager: Internal Audit should evaluate the responses, share the feedback, both positive and negative, with the internal audit team and take appropriate actions to continuously improve the quality of the internal audit work performed.
2. Perform an internal quality assurance review.
 - On a periodic basis, but at least annually, the Internal Auditor should perform a peer review on a sample of another Internal Auditor's files using the Internal Quality Review Checklist.
 - The sample size and frequency should take cognisance of the number of engagements for the year.
 - The files for review should be selected by the Internal Audit Manager.
 - The results of the reviews should be reported to the Internal Audit Manager and should be disseminated to the internal audit staff.
3. Perform an external quality assurance review.
 - An external service provider should be appointed by the Internal Audit Manager to perform an external assessment in intervals of not more than 5 years.

Templates

- ✓ Covering letter for Client Satisfaction Survey
- ✓ Client Satisfaction Survey
- ✓ Internal Quality Review Checklist

6.2 Follow-up of Previous Audit Findings

International Standards for the Professional Practice of Internal Auditing:

2500 – Monitoring Progress

"The chief audit executive should establish and maintain a system to monitor the disposition of results communicated to management."

2500.A1 – *The chief audit executive should establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action."*

2600 – Resolution of Management's Acceptance of Risks

"When the chief audit executive believes that senior management has accepted a level of residual risk that may be unacceptable to the organization, the chief audit executive should discuss the matter with senior management. If the decision regarding residual risk is not resolved, the chief audit executive and senior management should report the matter to the board for resolution."



Overview:

The purpose of adopting follow-up procedures is to support the mission of Internal Audit and reinforce the importance of controls in the Department/Program. Follow-ups provide management with updated information about whether important risks have been dealt with through remedial control actions.

Key objective:

- To ensure that management undertakes the necessary remedial action within the timeframe provided.

Key steps:

1. Establish a follow-up tracking system.
 - This system should include at a minimum:
 - Individual records on each recommendation contained in the internal audit report;
 - The name and contact information for the management official who agreed to implement the recommendation;
 - The original and revised target dates for implementation.
2. Obtain confirmation from management that all corrective actions have been implemented.
 - To ensure documentation of the correspondence is maintained, the request for a status of corrective actions should be communicated via a letter or e-mail. In the correspondence, management should be queried on the status of each recommendation, the reason why any recommendations have not been implemented if overdue, and new target dates for any recommendations which have not yet been implemented.
3. Determine the timing of the follow-up audit.
 - The timing of the follow-up of prior internal audit findings should be included in the Strategic/Operational Plan.
4. Develop a follow-up audit programme.
 - An audit programme should be drawn up which will provide the internal audit team with comfort that the action plans have been completely implemented to effectively address the risks identified.
 - The testing should be of a sample of 5. In determining the sample, consideration should be given to the following:
 - Where a portion of the sample selected cannot be tested because the recommendation is not applicable, the sample should be extended;
 - Depending on circumstances, the follow-up may require confirmation that the particular instances noted in the prior report have been addressed/rectified, as well as a new sample of 5 to confirm that the issue has not re-occurred.
 - The audit programme should be approved in the same manner as outlined in phase 2.
5. Perform the follow-up audit.
 - The follow-up audit should follow in the same manner as outlined in phase 3.
6. Compile a draft Follow-up Internal Audit Report to management.
 - A draft Follow-up Internal Audit Report is compiled following the same procedures as set out in phase 4.
 - The report format should be the same as for other audit reports, except the report should state that it is a report on a follow-up audit.



- The Follow-up Internal Audit Report should indicate the status of all previously reported recommendations i.e. whether they have been cleared, not cleared and or partly cleared.
- 7. Submit the draft Follow-up Internal Audit Report to the auditee for comments.
 - The draft Follow-up Internal Audit Report should be submitted to the auditee following the same procedures as set out in phase 4.
 - For those recommendations that have not yet been addressed, management should be requested to provide updated management comments including revised target dates for corrective actions.
- 8. Perform the final review of the Follow-up Internal Audit Report (incorporating management's comments).
 - The final review of the Follow-up Internal Audit Report should follow the same procedures as outlined in phase 4.
- 9. Prepare and issue the final Follow-up Internal Audit Report to the auditee.
 - The preparation and issue of the Follow-up Internal Audit Report should follow the same procedures as outlined in phase 4.


Follow-up audits are treated as an engagement and therefore all the necessary audit steps should be completed.


Templates

- ✓ Covering Letter for Follow-up Audit Report
- ✓ Follow-up Audit Report



7. APPROVAL


_____: Internal Audit Manager
Mr. M Nishangase
05/06/17
Date


_____: Municipal Manager
Mr. GM Simeke
05/06/17
Date


_____: Audit Committee Chairperson
Dr. PS Zulu
05/06/17
Date