UMZIMVUBU LOCAL MUNICIPALITY
OFFICE OF THE MUNICIPAL MANAGER

INTERNAL AUDIT METHODOLOGY AND PROCEDURE MANUAL
2021/2022

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1. INTRODUCTION

Umzimvubu Local Municipality: Internal Audit Unit (hereinafter referred to as ULMIAU) is "an independent, objective assurance and consulting activity designed to add value and improve Municipality operations. It helps municipality to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes".

ULMIAU**' Business Objectives are to:**
- provide assurance that the control environment within areas reviewed is adequate to manage the related risks within acceptable limits and at reasonable cost;
- provide expertise and advice regarding improvement of the existing risk levels, controls, processes and/or outputs, either by recommendations in reports, or through direct facilitation in a consulting capacity;
- provide continuous contribution to the improvement of risk management and control systems, through reports and recommendations;

Assurance and Consulting Services

The provision of assurance and consulting services on the adequacy and effectiveness of risk management, control and governance processes to the stakeholders is the primary objective of ULMIAU.

This is achieved through:
- identifying, evaluating and assessing significant organisational risks and exposures relating to Umzimvubu Local Municipality's operations as well as information and communication systems;
- monitoring and evaluating the effectiveness of Umzimvubu Local Municipality risk management strategies;
- evaluating the effectiveness and efficiency of the related internal control systems; as well as
- Ascertaining the extent to which established goals and objectives conform to those of the organisation and are consistent with Umzimvubu Local Municipality's organizational values.

2. PURPOSE

The purpose of this document is to provide guidance on the procedures followed in the performance of internal audit services, namely: Assurance and Consulting Activities.

The objectives as well as the procedures followed for each section are explained with reference to the International Standards for the Professional Practice of Internal Auditing as well as international best practice.

These guidelines have been designed to be sufficiently flexible so that they can be changed to suit dynamic circumstances. Authority and guidance should be sought from the Manager: Internal Audit.

3. AUDIT PROCESS

Audit work is performed to provide management with reasonable assurance regarding the design and implementation of internal controls. The council and management are responsible, inter alia, for establishing and updating business objectives and goals, implementing and maintaining cost effective systems of internal control and ensuring that these business objectives are achieved, by developing and maintaining an environment that fosters control and mitigates risks.

The audit process includes Planning, Fieldwork, Reporting and Follow up (Continuous Monitoring).

3.1 PLANNING

The primary role of ULMIAU is to assist management to accomplish the municipal objectives by providing independent, objective assurance and consulting activities by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Three year rolling plan
The municipal three year rolling plan is derived from an independent enterprise-wide risk assessment comprising macro and micro risks affecting Umzimvubu Local Municipality environment. This plan is implemented and executed annually, in recurring cycles.

The plan is reviewed annually following an independent risk assessment by ULMIAU to determine the focus and delivery of the assignments undertaken and to realign the following years planned cycles. The plan incorporates clients, external auditors and relevant stakeholder inputs. The plan is completed and tabled for discussion and approval at the Audit Committee Meeting.

Annual audit operational plan
The annual audit plan is derived from the three year rolling plan, taking into account specific client requests, the existing environment and available resources

The annual audit coverage plan is broken down into various quarters (cycles), from which individual assignments (audit projects) are allocated. ULMIAU further undertakes special projects as identified during our annual audit coverage or at the request of relevant department.

The annual audit plan reflects, among others the following:
• Auditable entities;
• Level of risk;
• Last audited date;
• Control environment (Design of controls); and
• Management of risks (Implementation of controls).

Project allocation

After the annual audit plan has been prepared, Internal Audit management allocates work to available resources taking into account timing and skills required. The project allocation is then which reflects the following:

• Project Number;
• Year;
• Cycle;
• Project Manager;
• Auditor;
• Audit Activity;
• Type of Audit;
• Hours Allocated; and
• Start and Finish Dates.

The Audit project needs to be registered on the project library and a project number allocated prior to commencement. The project numbers are allocated in advance using the following prefixes, sequential number and the financial year e.g. 01/2022.

Pre-engagement activities
• **Engagement Letter**

The engagement letter is designed to advise the Department to be audited of our intention to conduct an audit in his/her area of operation. The engagement letter will include the scope and primary objectives of the audit and to introduce the key members of the audit/project team. This letter must be sent out at least one week prior to the commencement of fieldwork of any planned project. Earlier release of the engagement letter is encouraged (i.e. at the beginning of the quarter in which the project will occur).

The engagement letter should be written to the Senior Manager of the Department being audited with the Manager of that division being copied.

- **Preliminary survey**

Team Briefing

The team leader will inform the team members of inter alia the following:

- Discussion of Audit Planning Memorandum
- Critical issues identified during the planning stages of the audit/project;
- Their responsibilities and agreement on performance; and
- Logistical arrangements.

Information Gathering

An understanding of the operations of the business unit being audited is fundamental to proper audit/project planning and execution. It is essential that sufficient information be obtained about the business unit to be able to assess the environment, in which it operates, the organisational structure of the relevant business unit, including related dependencies that are affected by the process being audited. This information is vital in identifying areas of high risk, formulating audit/project programmes. Information to be gathered generally includes:

- Background information about the business unit's operations, goals and objectives;
- Descriptions of the information, accounting and control systems;
- Policies and procedures;
- Information specific to the business unit's current activities and plans and expectations for the future;
- Operational process flows and descriptions;
- Reporting requirements/ terms of reference;
- Applicable Laws and Regulations;
- Organogram for the business unit; and
- Prior audit reports and working papers.

Information gathering should be conducted prior to submission of the APM to the client at the opening conference meeting.

- **Audit Planning Memorandum (APM)**

Once the above information has been obtained, the Audit Planning Memorandum is prepared. The purpose of the APM is to set out why the audit is being done, what risks and processes it will involve, what it will deliver how it will deliver, who will deliver and when they will deliver. The APM forms a basis for "Professional Courtesy" and engagement of the client in areas under review with a view to appreciating and/or documenting specific risk areas the client considers appropriate in addition or prioritization of urgent issues. This APM is signed as acknowledgement of acceptance and client commitment to the audit process.

The APM should be discussed with the audit team which will be involved in the audit, reviewed and approved by the Manager: Internal Audit at least one week before the audit commences and, after being discussed with the client, signed by the Manager at the opening meeting. As the scope may cross departmental and functional areas, special consideration must be given regarding who should be included on the distribution list.

The APM should include details such as:
- The objective of the project;
- Audit scope of coverage;
- The period covered by the project;
- Approach;
- To whom the audit report will be distributed;
- Staffing for the project;
- The expected time to be spent on the project; and
- Estimated commencement date, discussion of Record of Audit Findings (RAFs) date and issue date.

The Manager: Internal Audit should determine appropriate resources to achieve the engagement objectives. This decision should be based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

Subsequent changes that affect the timing or reporting of engagement results should be communicated to client management, if appropriate. These changes are subject to written approval from the Manager: Internal Audit.

Opening Conference Meeting
The opening meeting should be held between the department Senior Manager; Manager Internal Audit and the Manager in charge of the audit project. Details of the engagement can be worked out during this preliminary meeting as well as establishment of a cooperative tone for the audit, which will follow. It should be made clear to the management team of the department being audited that the Manager Internal Audit will keep them informed and update them on the status of the audit.

During this meeting, the following should be discussed:
- Current status of prior audit findings;
- Objectives and Scope of the audit project;
- Time, extent and nature of audit project;
- Discuss and agree with the client on the tolerable error rates and risk (exposure) ratings;
- Client's input regarding problem areas where auditors can be of assistance to management. (Careful consideration should be given to any suggestions from the client. Auditors should not become involved in functional or operational activities.);
- Audit findings - (Explain how audit findings will be handled, e.g., resolution of minor findings, the discussion of all findings on an ongoing basis to permit the client to take timely corrective action.);
- The frequency of progress updates and management levels to be informed of audit progress and findings;
- Timing of the closing meeting;
- Distribution of the final audit report;

- Co-operative administration – Inquire about working hours, access to records, available work area for participating auditors, the client's various work deadline requirements, and any other information which will help schedule the audit project activities to fit into the office routine with minimal disruption to the client personnel;
- Arrangements to meet other personnel the auditor will be working with during the audit;
- Arrangements for a familiarization tour of the physical facilities;
- Request to complete the post audit questionnaire at the end of the audit; and
- Assistance to obtain specific information required during the audit, e.g. process flow documents, policies, procedures, etc.

- **Systems Documentation**

Systems documentation refers to the process of systematically documenting one's understanding of the processes and their control systems. The primary purpose of preparing system documentation is to identify, analyse and understand the business processes/systems, procedures, the risks and internal control objectives involved in operations. It is important to consider the cost effectiveness of the method used to document the systems. Systems documentation may take on various formats i.e.

- Flowcharts;
- Narratives;
- Extracts of procedures manuals, etc.

Flowcharts

The primary purpose of preparing a process flow (flow chart) is to identify, analyse and understand the business processes/systems, procedures, the risks and internal control objectives involved in operations. This pictorial method can efficiently highlight instances of under/over control and redundancy.
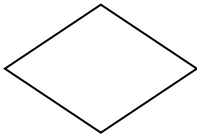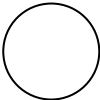
The auditor usually obtains information necessary for preparing or updating flow charts by interviewing personnel at the business/process about procedures followed, and by reviewing procedure manuals, existing flowcharts and other systems documentation.
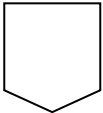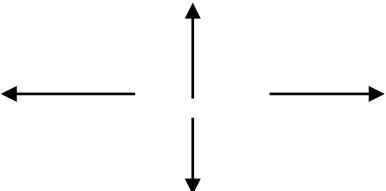
Flow charts should at least comply with the following requirements:
- Be prepared uniformly, logically, concisely and clearly.
- Be broken down into its components (e.g. actions and decisions).
- Indicate the position(s) of the people performing the transactions/actions.
- Include the "name" of each document (e.g. IB143) within the appropriate flow chart symbol. An explanation of the "name" must be provided as a glossary to the working paper.
- Processes usually flow from top to bottom and left to right in the flow chart.
- Action verbs should be used in the flow chart.
- Use connector symbols (on-page and/or off page) rather than drawing lines around or over parts of the flow chart.

The following are the basic flow charting symbols and flow lines to be used:

Symbol	Description
Document	Input or output in the form of a document or report.
Process	Processes or operations followed.
Manual process	Manual processing operation, e.g. keypunching
Input / Output symbol	Generalised symbol for input or output.
Decision Symbol	Indicates a decision process within the flow chart. From the decision symbol, different options to follow should be indicated, e.g. decision is whether a return signed, leading to a yes or no output.
On-page Connector	Connection between points on the same page.

Symbol	Description
Off-page Connector	Connection between two pages of the flow chart.
Direction Arrows	Indicates the flow direction of processes.

Narratives

Narratives document the activities within each process in detail. The purpose of this is to assess the effectiveness of the organisation's risk management process and related internal controls, by means of discussions with management and staff.

The narrative can take various forms including;

- One on one interviews

    The auditor sits with the client and interviews him/her about each activity within the division;

    - o Upon documenting the systems, the auditor needs to confirm the documented system with the client;
    - o The client needs to sign off the narratives confirming that they are true and correct.
- Risk assessment workshops;

    o The main aim of the risk assessment workshop are to confirm objectives, re-assess previously identified risks, identify the strategic risks threatening the achievement of these objectives and prioritise the newly identified risks.

    - o During the workshop, management participation will be required to provide inputs based on their actual knowledge and experience of their functions and environment.
- Questionnaires filled in by the organisation.
    - o For compliance the Control Self-Assessment (CSA) questionnaire is sometimes used to get the business units to assess themselves on their level of compliance.
    - o CSA is a process through which internal control effectiveness is examined and assessed. The objective is to provide reasonable assurance that all business objectives will be met.

Where considered appropriate, the documentation of systems should be performed incorporating the following techniques:
• Inquiries and observations with functional staff and management.
Conducting walk – through tests (i.e. following a transaction or process from the point of initiation to the point where it is executed and recorded to ensure that the system is operating as described).

Whatever the method used to analyse the function/process, it is critical that as a minimum the above objectives/details are clearly identified and form the basis of the internal audit programmes and the work performed.

• **Risk and Control Matrix**
The detailed risk matrix is a systematic process of identifying and rating risks as well as identifying and assessing controls. This process provides a means for providing an opinion on the adequacy of the controls based on professional judgment and developing the audit program for effectiveness reviews. Higher risks should be given priority; however medium and low risks should not be excluded from the detailed audit program.

Information incorporated into the risk matrix should be obtained from a variety of sources such as,
• Information obtained in the planning phase;
• Control weaknesses (risks) identified during the drafting of the systems documentation;
• Benchmarking the process against best practices; and
• Brainstorming the process in order to identify risks.

Steps to be followed in the risk assessment process to formulate an opinion on the adequacy of the process being audited are the following:
• Identifying risks;
• Measuring risks;
• Identifying Controls; and
• Assessing the Adequacy of Controls.

Identifying risks
A risk is the uncertainty of an event occurring that could have an impact on the achievement of objectives. Based on the system documentation, identify and note potential risks that might have an impact on the client's performance and prevent it from reaching its objectives.

Assessment of risks
For each risk identified, assess the potential impact on the client's performance (achievement of objectives) and the likelihood of the risk occurring. Risk is measured in terms of impact and likelihood.

Impact

Impact refers to the exposure if risks were to occur. Auditors should consider the impact that the undesired event will have (in the event that it does occur) on the organisation.

Likelihood

Likelihood is the probability (considering the present control environment or action in hand) that an adverse event, which could cause materialization of the risk, may occur.

It is suggested that the auditor assesses the overall impact and likelihood of the risk using a measurement scale of high, medium and low as indicated below:

Risk Severity of Impact:	*Likelihood of risk event occurring*			
	Unlikely <15%	*Fairly likely*	*Very likely*	*Almost certain >85%*
1.Minor impact on payroll payment /No Impact – fraud/invalid payments	Low	Low	Medium	Medium
2.Minor Impact on fraud/invalid payments	Low	Medium	Medium	High
3.Major impact on payroll payments	Medium	Medium	Medium	High
4. Major impact on payroll payments	Medium	Medium	High	High
5.Major impact re fraud/invalid payments	Medium	High	High	High

Identifying Controls

Based on the system documentation, identify the relevant controls in place to mitigate the specific risks to an acceptable level. Policies and procedures should be interrogated to find appropriate controls. There are three types of controls that management can put in place, which are:

• **Preventive Controls** are the controls put in place prior to materialization of the risk in order to prevent it from materializing.

• **Detective controls** are the controls put in place after materialization of the risk to identify it and prevent it from re-occurring.

  Directive controls are controls that are put in place as a requirement such as compliance controls.

Assessing Adequacy of Controls

To assess the adequacy of the existing controls for each significant risk (best practice), the auditor should ask whether the controls will, if adequate, reduce the potential impact of the risk to an acceptable level for the business unit/division.

The question should be asked: "Do the controls effectively reduce the likelihood of the risk occurring and, should it occur, would they effectively minimize its impact?"

Evaluating the answers requires the auditor's professional judgement and knowledge of generally accepted management practice.

The controls assessed should be rated "Adequate", "Needs Improvement" or "Inadequate" based on whether they will assist management in achieving their objectives. Colour coding should be used to make the assessment more visible, RED to be used for "Inadequate"; YELLOW to be used for "Needs Improvement" and GREEN to be used for "Adequate" controls.

Adequate

A control is adequate if it reduces the risk identified to an acceptable level and will therefore assist management in achieving their objectives. For adequate controls an audit programme is designed to test the implementation of the control (effective, efficient and economical).

Needs Improvement

Control is said to require improvement if it is in place, but is not sufficient to reduce the risk to an acceptable level and will therefore partially assist management in achieving their objectives. For needs improvement controls an audit programme is designed to test the implementation of the control (effective, efficient and economical).

Inadequate

A control is inadequate if it does not address/ reduce the risk identified to an acceptable level and will therefore not assist management in achieving their objectives. Inadequate controls are not tested at all for implementation, the report is prepared and appropriate recommendations made (refer to reporting below).

Controls to provide reasonable assurance of the:	Control Adequacy	Control Implementation	Trend
Implementation and utilization of assets module	😐	😐	N/A
Overall Audit Opinion	😐	😐	N/A
😊- Adequate/Effective 😐- Requires Improvement ☹- Inadequate/Ineffective *Trend = either improving; neutral; deteriorating or N/A= not available*			

Audit Programme

Based on the areas identified as adequate and/or needs improvement in the detailed risk matrix, a detailed audit programme needs to be developed to test the implementation of the controls identified for effectiveness, efficiency and economy. The main objective and purpose of the audit program is to verify the controls that were identified as adequate that are effective, efficient and economical in order to assist management to achieve their objectives.

It should address only what is significant and give proof to the fact that significant risks and controls were identified and evaluated.

The detailed audit programmes should clearly set out the audit objectives and the audit procedures to address the objectives identified. This is to ensure that audit objectives and procedures are risk based and focus on areas that could result in significant exposure to the business unit if the respective controls are not operating effectively.

Upon completing the audit programme, it must be submitted to the Manager Internal Audit for review. No audit program should be executed unless it has been reviewed and approved by the Manager Internal Audit.

Administrative Planning

Prior to commencement of the project the team leader/ auditor should ensure that all the required resources have been organised and are available. The following are examples of the resources that must be organised:

- o Laptops;
- o Team members;
- o Files;
- o Stationery;
- o Office space;
- o software requirements
- o S & T.

3.2 EXECUTION GUIDANCE

Execution is the process of examining and evaluating information, systems and processes, furthermore it may also mean putting into effect the audit program, under an ongoing cycle of monitoring, control and communication by the project leader/ manager. During this phase, the auditors will be practically implementing the audit work program, "getting out and doing the job."

Fieldwork takes various approaches including; observations, interviews, examining and corroborating documentation, data and information analysis, re-performances and recalculations, sampling, testing of controls, questionnaire, etc. The approach undertaken relies on a range of verification and observation procedures deemed appropriate to allow ULMIAU to independently and objectively comment on the control environment and management risk by the auditee. The internal auditor is not restricted nor limited by any procedures to the number or kind of approaches to be used. Any approach or combination to be used is determined by the nature of the assignment and the results required.

Fieldwork may be performed in various places and environments such as; in facilitated workshops, one-on-one meetings, auditors' and/or auditees' offices, virtual workstations and systems testing servers, desktop reviews, investigation and/or use of control self-assessment questionnaires (CSA).

Sampling

The sample selection (number of cases/transactions) needs to be free from bias and sufficient to support an audit opinion that the controls are working as intended or not.

A maximum selection of 25 samples must be made to be subjected to audit tests. Depending on the tolerable and expected error rate, an additional sample needs to be selected where an error is identified, as to assess whether such error is an isolated incident, or whether it is a breakdown in the system of internal control (i.e. controls are working effectively or not).
Note that it should be ensured that each audit test should be performed on the complete sample size selected. Therefore if the sample size is 25, 25 items need to be selected for each test (thus if the audit program consists of 10 tests, each test will be conducted 25 times).

In the case of financial audits, the sample size needs to be representative of the total population of transactions out of which the account balance tested consists. The most common method used to perform this is a statistical method, whereby the sample size is mathematically calculated based on the total population of the transactions and the figure, which has been determined as material.

The following sampling table should be a guide when testing a sample to ensure fair presentation of the population in our sample. This table should be given a high consideration in all audit projects undertaken to enhance external auditors' reliance to our work:

Frequency of operation of the control	Minimum sample size	Extended sample size
Annual	1	0
Quarterly	2	3
Monthly	4	6
Weekly	15	20
Daily	30	40, 50
Multiple times per day	30	40,50,60

Collection of the sample
- The Auditor should collect the requested sample from the auditee for the purpose of testing.
- The collected documents should be signed for by both the auditee and auditor to ensure accountability, e.g. these signed documents could be used for evidence of inadequate safeguarding of documents.
- The Auditor should take full responsibility for custody of all collected documents for testing until the end of fieldwork.

- Upon satisfactory conclusion of fieldwork the sampled documents should be returned to the auditee and compared to its initial request schedule for completeness and be signed for by both the auditee and auditor.

Working papers

Auditors should prepare working papers, which record the information obtained and the analyses made in planning and conducting an internal audit. In addition the working papers "should support the basis for the findings and recommendations to be reported".

Proper working papers demonstrate professionalism and document the work that was performed from the preliminary stages of an audit project through to the final report. Audit working papers also show whether due professional care was exercised and illustrate compliance with professional auditing standards.

This section contains characteristics of well-organized and documented working papers and should be used in evaluating the adequacy of working papers. Careful documentation of work performed is necessary to support the findings, recommendations, and opinions contained in the final audit report.

Working papers should contain sufficient information to allow an experienced auditor having no previous connection with the audit to ascertain from them the evidence that supports the auditors' significant conclusions and judgments.

Purpose of working papers

The primary purpose of working papers is to provide details to prepare the report and they also serve the following purposes:
- provide evidence that audit standards have been followed;
- assist in planning, supervising and performing the audit;
- assist reviewers to understand the work performed during the audit;
- documentation of information obtained about the area being reviewed;
- authoritative support for findings and recommendations contained in the audit report;
- uniformity to the audit process;
- a means of evaluation - both auditor performance reviews, including the standard of work produced and quality assurance reviews; and a guide for subsequent audits.

Working paper guideline
To prepare a professional working paper the following guidelines should be taken into consideration:

o **Completeness and Accuracy** - Working papers should be complete, accurate, and support observations, testing, conclusions, and recommendations. They should also show the nature and scope of the work performed;

o **Clarity and Understanding** - Working papers should be clear and understandable without supplementary oral explanations. With the information the working papers reveal, a reviewer should be able to readily determine their purpose, the nature and scope of the work done and the preparer's conclusions;

o **Pertinence** - Information contained in working papers should be limited to matters that are important and necessary to support the objectives and scope established for the assignment

o **Logical Arrangement** - Working papers should follow a logical order; and

o **Legibility and Neatness** - Working papers should be legible and as neat as practical. Sloppy s may lose their worth as evidence. Crowding and writing between lines should be avoided by anticipating space needs and arranging the working papers before writing.

Working paper structure:
ULMIAU working papers should at least contain the following items:

Paper Size - Audit working papers should be presented on the A4 MS Excel spreadsheet.

Heading - Each working paper should have a descriptive of the following:
• Umzimvubu Local Municipality;
• Area Audited e.g. Process – Budget and Treasury, Sub-process – Supply Chain Management;
• Project Code e.g. 15-2016; and
• Review period e.g. 01 July 2019 to 30 June 2020

Initials/Date - Each working paper should be dated and initialled by the preparer; the reviewer should mark and date the working paper to show that it has been reviewed and approved. In the case of the Audit software a preparer must sign off all her/his working papers so as to allow the reviewer to review his/her work.

Audit Tests
Audit tests (i.e. audit objectives and audit procedures) should be copied from audit programme document, and be pasted to working papers and be aligned accordingly. For each sub-process tested a separate working paper should be created (e.g. Segregation of Duties, Annual Leave, Policies and

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Procedures). If necessary a table listing selected transactions or items should be created and be aligned to the audit programme.

Extent of evidence

During execution the auditor will obtain audit evidence to support his/her opinion on the adequacy and effectiveness of controls. Audit evidence is obtained through the following techniques:

Technique	Procedure	Explanation
Observation	Test of control	Direct viewing of the client management and staff in their work environment.
Enquiry	Test of Control	Making specific enquiries of client management and staff, in sufficient depth.
Confirmation	Test of control	Enquiry from third parties.
Inspection of evidence	Test of control	Inspection of records, documents, reconciliations and reports for evidence that a control procedure has been properly applied.
Analytical procedures	Dual test (Both test of control and substantive test)	Comparison of financial information with similar information (internal or external)
Re-performance of the control procedure	Dual Test	Repeating a control procedure performed originally by the client or a computer program.

Testing techniques for obtaining evidence

Observation

The auditor should use caution in extending observation conclusions, because personnel may be appropriately performing procedures only at the time of observation. Therefore, additional techniques should be used to support the observation conclusions reached. Observation is often employed for controls that cannot be tested through inspection.

Enquiry

Evidence obtained through enquiry should generally corroborate other forms of evidence. The auditor should ensure that the procedures he/she follows are sufficiently comprehensive to support the assessment of the control. In making enquiries, you should question the individual to obtain a full understanding of how effectively the control is performed. Be alert to vague or glib answers and to apparent inconsistencies.

Confirmation

Confirmation provides the auditor with evidence, directly from third parties. Confirmation is a useful audit procedure for a number of audit objectives, because it provides strong, documented evidence from an independent, external source. Confirmation should only be requested, in respect of information, to which the respondent can reasonably be expected to be knowledgeable.

Inspection of evidence

The auditor should obtain evidence of the performance of a control procedure. Evidence may include:

- Written explanations;
- Indications of performance on a copy of a report or document used in the control procedures; and
- Evidence of follow up action where this is warranted.

Absence of evidence may indicate that the control procedure is not operating as prescribed, so further enquiries will be necessary if it is to be accepted that there is in fact an effective control.

The following are additional inspection techniques:

- **Footing** of transactions – refers to adding figures contained in documents in order to compare the document totals with those calculated by the auditor;
- **Reconciling** – refers to showing mathematically, with supporting documentation, the changes in beginning and ending totals;
- **Vouching** – refers to examining the underlying written evidence to support final reported amounts;
- **Verify and determine** – refers to ensuring that particular activities, amounts, procedures, etc. are as they are represented to be; and
- **Evaluate** – refers to judging the quality of internal controls.

Analytical procedures

Analytical review procedures are normally carried out by studying and comparing relationships between related sets of data. If controls are determined to be effective and the area is not deemed critical, analytical review procedures, corroborating the recorded data, may be sufficient. If however, the area is deemed critical, substantive procedures in addition to analytical review will generally be required.

Re-performance

The auditor should normally consider re-performance only when observation and enquiry, supported by inspection of evidence does not provide sufficient assurance that the control is operating effectively. Sometimes, a control is of such significance that you should obtain further evidence of its effective operation, because there would be serious consequences of misstatement if it were not operating effectively.

If re-performance is used, the extent of re-performing required is a matter of judgement. If the auditor needs to carry out extensive re-performance of control procedures to gain the required assurance, he/ she should consider whether it is more efficient to perform substantive test procedures.

Adequacy of Evidence

Evidence included in working papers should be sufficient, competent, relevant, and useful to provide a sound basis for audit findings and recommendations.

- **Sufficient** information is factual, adequate, and convincing so that a prudent, informed person would reach the same conclusions as the auditor.

- **Competent** information is reliable and the best attainable through the use of appropriate audit techniques.

- **Relevant** information supports audit findings and recommendations and is consistent with the objectives for the audit.

- **Useful** information helps the organisation meet its goals.

Evidence of all critical matters (whether right or wrong) should be kept on the audit file. Policies and procedures should be interrogated to find appropriate controls. Specifications for Application systems should be reviewed to find controls and these controls should be tested on a development / test environment. The source of the control, e.g. policy, law, etc. should also be indicated, if possible.

Tick marks

Tick marks are used to simplify documenting work done and conditions found, usually during fieldwork. A legend that defines each tick mark should be provided and located near the tick marks used. If the tick mark legend is not on the working paper where the tick marks are used, the working papers should be referenced to the tick mark legend. E.g. **X test result unsatisfactory**

Tick marks should be concise and should adequately explain the results of the audit procedure performed. It should be evident as to whether or not an error or weakness was noted. Items tested should never be left blank, the results of the test should be documented, the attribute should be marked as not applicable, or an explanation should be provided as to why the test could not be performed. Explanations should be provided to show why items marked "N/A" are not applicable.

Content of the working paper

For every audit program step, working papers should contain a summary of the results of work performed and a conclusion about these results.

For internal control and workflow evaluations, conclusions should address the adequacy of the system or process, that is, whether the design of the system contains the features needed to provide reasonable assurance that management's objectives will be met. The conclusion should appear at the end of the control narrative.

Conclusions about test work should address whether or not the expected controls or processes identified in the review of internal controls or work flows are effective. If there is room, the summary and conclusion can be placed on the working paper that documents the test work.

In both cases, the conclusion should identify the overall significance of any weaknesses or exceptions found.

Opinion should be expressed for each sub-process tested (i.e. adequate, inadequate, effective and/or ineffective).

Avoid including multiple copies of an item in the working papers or any item that is not needed to support the work performed and the findings and conclusions in the audit report.

Referencing
Each page in the working paper should be given a unique reference number that identifies its location. The number assigned should begin with a capital letter that matches the section of the working papers where the page will be filed followed by a dash and a number that allows the page to be filed in a logical sequence. If a working paper continues for multiple pages, or if there is evidence supporting a working paper, subsequent pages and the evidence should have the same letter and first number identifier followed by a lower case letter or by a period and another number.

This approach provides a way to logically link related working papers and gives enough flexibility for pages to be added as needed. This approach should be applicable to all working papers in the file (Both Working and Permanent File) and no audit project should be declared as "Complete" without proper referencing.

A good indexing system for working papers should be simple and easily expanded, whilst effective cross-referencing facilitates supervisory review, finding information in the working papers and finalization of the audit report.

Supervision

The execution phase of the audit project should be properly supervised to ensure that objectives are achieved and quality is assured. Care should be taken that record of audit findings (RAF) /exceptions raised and recommendations made are relevant to the business objectives and that value will be added to the business.

Supervision by the audit Project Manager includes:
- review of all the work programs (100%) daily and/or weekly
- providing coaching (review) notes;
- follow-up on progress of the coaching (review) notes issued; and
- ensure that all coaching (review) notes are cleared prior to the completion of the audit.

3.3 REPORTING

Internal Audit's core role in reporting is to communicate the results of audits to the Audit Committee and Management by expressing an opinion on the adequacy of design and implementation of controls. Where the opinion states controls to be ineffective, the onus is on management to implement the appropriate controls.

Adequacy Opinion
The adequacy opinion seeks to provide an opinion on the design of controls created by management. The following faces are used in the Audit Committee report to represent opinion per each process for the period audited:

☺ **- Adequate;** 😐 **- Needs Improvement; and**

☹ **- Inadequate.**

Effectiveness/Implementation Opinion
The effectiveness opinion seeks to provide an opinion on how well the controls have been implemented by management and staff to mitigate the risks identified in operations. The following faces are used in the Audit Committee report to represent opinion per each process for the period audited:

☺ **- Effective;** 😐 **- Needs Improvement; and**

☹ **- Ineffective.**

In its simplest form, reporting is the communication of the review results. The reporting process begins within the fieldwork stage in various forms and becomes stricter subsequent to the fieldwork. The reporting process undergoes various stages. These are called Records of Audit Findings (RAFs) workshop phases. This document is used to record findings. The objective of this file section is to collect report points in a single section of the Audit Working Papers file.

Always remember that the audit report *(Annexure K)* is our product that we sell, and against which we are evaluated. Therefore it must always maintain a high standard of quality and professionalism directly linked to the high standard and professionalism of our audit work.

A report quality assurance review should be performed on the report before discussions with the client.

The report should comply with the following criteria:

Accuracy - The auditor must always keep in mind that the report must be completely factual. Every statement, every figure, and every reference must be based on hard evidence. Statements of fact must carry assurance that the auditor personally observed or validated every fact stated in the report.

Objectivity - Objective communication should be fair, impartial, and unbiased and is the result of a fair-minded and balanced assessment of all relevant facts and circumstances. Observations, conclusions, and recommendations should be derived and expressed without prejudice, bias, personal interests, and undue influence of others.

Clarity - Clear communication should be easily understood and logical (e.g. inadequate transitions between paragraphs, thoughts, and conclusions). Clarity can be improved by avoiding unnecessary technical language and providing all significant and relevant information.

Conciseness - Concise communication should be to the point and avoid unnecessary elaboration, superfluous detail, redundancy, wordiness and too many ideas in a single paragraph. They are created by a persistent practice of revising and editing a presentation. The goal is that each thought will be meaningful but brief.

Constructive Tone - Constructive communications should be helpful to the client and the organization and lead to improvements where needed. The contents and tone of the presentation should be useful, positive, and well-meaning and contribute to the objectives of the organization.

Complete - Complete communication should be lacking nothing that is essential to the client and include all significant and relevant information and observations to support recommended actions and conclusions.

Timely – Communication should be well-timed, appropriate, and expedient for careful consideration by those who may act on the recommended actions. The timing of the presentation of results should be set without undue delay and with a degree of urgency so as to enable prompt, effective action.

Tense – The report should be written in the past tense.

Formal Tone – The report is a formal means of communication, therefore when reference in the report is made to people, they should be referred to as Mr/Ms as well as their designation should be indicated.

Record of Audit Findings Workshop

As a practical focus to encourage practical engagement by officials and limit common client delays in responding to audit queries, and management actions, to facilitate speedy delivery of audit work, the Record of Audit Findings (ongoing) workshop (RAF's) is undertaken at various levels. This is the initial stage of our reporting process and the RAF templates are used as a basis of discussion. The report is not yet documented, only audit queries known as management report points (MRP). The aim of this stage is to perform accuracy verification. The findings arising are communicated to the Departmental Manager and the Assistant Manager concerned in order to obtain management comments.

The MRPs are the findings arising which the wording thereof is subject to change/modification following the discussions. This stage also allows the revision of some of the audit queries provided the relevant documentation, evidence or secondary effective controls that may have not been detected during the review are provided.

This phase provides management an opportunity to respond to the raised findings and the relevance of audit findings in the report. However, management should bear in mind that the findings of the report will only be changed or removed when evidence is produced for the findings concerned or complimentary controls are identified.

Management is allowed seven (7) days to provide management comments, failing which the report will be issued without management comments and managers will be required to provide written action plans within a timeframe of ten (10) days.

At this stage the RAF's would have undergone a Quality Assurance process in which, the Assistant Manager: Internal Audit would have reviewed, prior to RAF's being discussed with the Managers concerned

Subsequent to the discussion with the Management, the report is converted from the draft report to the final report and issued. In the case of Umzimvubu Local Municipality it is at this stage that the Municipal Manager would join in as the process recognises responsibility and accountability as defined by MFMA.

NB: After ten days of waiting for final comments and action a report is finally issued by the Manager: Internal Audit after Quality Review (QAR) considerations.

In the event of a disagreement, ULMIAU will consider reviewing the situation, decide whether reference should be made to the disagreement in the final report or whether the disagreement should be escalated further, first to the Municipal Manager and then if necessary, the Audit Committee.

The executive summary of the report containing only significant issues is discussed with the Senior Managers or Managers. The communication is for securing action and information purposes and highlighting the high risk areas in all areas reviewed within Umzimvubu Local Municipality.

You may have realised by now that the communication process is not restricted to reporting, but takes place throughout the entire review process from planning to the conclusion of the assignment. An effective communication is the critical element of a successful review.

Draft Reports
Draft reports may be used to:
• communicate information which requires immediate attention;
• communicate a change in audit scope for the activity under review; and/or
• Keep management informed of audit progress when audits extend over a long period."

The Assistant Manager Internal Audit should review the work currently completed and issue a report, a copy of which is kept in its specific section of the working papers file. The report in this phase contains a draft watermark "DRAFT"

In terms of best internal audit practice there should be continuous dialogue and communication between the auditor and management regarding the status of the audit and relevant findings. Notes of formal discussions and meetings should be kept in the internal audit file.

The only exception to this will be in a situation where the project is to investigate fraud and/or embezzlement and the perpetrators and full extent of the fraud is unknown. In these cases the report will only be submitted to the relevant management of the organisation audited.

How to complete and use the "Record of Audit Findings" The purpose of this section is to record and report:
• the findings, observations and potential risks identified during the audit project;
• the recommendations to correct errors and/or address potential risks;
• the comments of client management regarding the findings and recommendations; and
• the agreed client management action plan to counteract the risks, detailing when the action will be implemented and by whom.

As report points (exposures; weaknesses, errors, etc.) are identified during the course of the audit and recorded in the working papers, they should also be included in and cross referenced to this section. This will improve control over report points and facilitate the review process.

Business Activity

This section lists the Business Activity as it appears in the Risk Matrix document.

Standard

This is a brief (one line) summary of the actual finding to provide the reader with an indication as to the subject of the report point.

Condition

All weaknesses and errors identified during the audit process will be documented and reported to management, whether financially immaterial or not. Often an error or weakness in principle does not have significant financial impact, but is still material - because a fundamental control/policy principle has been undermined.

Findings "emerge by a process of comparing what should be [the criteria] with what is [the condition]"

Findings, therefore, constitute the difference between the criteria or "*what should be",* for example:
- good business/management practices;
- generally recognised accounting practice;
- generally accepted accounting practice;
- internal/departmental standards, policies and procedures;
- relevant legislation; previous audit experience (which will add value and illuminate the situation); and
- the condition or "what actually exists" (i.e. the actual events surrounding the situation or circumstances).

Based on your professional judgement, decide whether (and how many) examples of the weaknesses identified, should be noted. The advantages and disadvantages of noting the examples should be considered carefully. The noting of examples can either give more prominence to the finding or result in management only correcting the noted examples.

In completing this section of the document, the auditor should evaluate the audit evidence to assess if what actually exists is what should be in place. Each difference should be recorded on the specific working paper and on an individual schedule of findings and recommendations.

Cause

The audit finding should be discussed with the client in order to determine the root cause and possible corrective actions (recommendations). The root cause should indicate the causes for the condition and if addressed should limit, minimise and eliminate the risk.

Potential Risk and Effect

If the condition is different from the criteria, the Division may be exposed to a risk in that area. The potential risk is recorded in this section of the document.

A potential risk / implication could relate to either;
- the risk of loss to the organisation; or
- the risk of an opportunity/or gain not being taken up by the organisation; or
- the risk of not complying with legislation, departmental policies and procedures; etc.

In paragraph format, indicate the risk that might materialise if the control is not properly managed / the recommendation implemented / corrective action taken. The statement should indicate the potential impact that the client (and/or organisation) encounters because the condition does not meet the criteria (root cause is not addressed).

The potential risk/implication can be determined through knowledge of good business/management practices, generally recognised accounting practice, generally accepted accounting practice, internal departmental standards, policies and procedures, relevant legislation and previous audit experience.

Recommendation
When the potential risk/implication has been identified, the auditors should recommend actions to correct the error, reduce the risk exposure or improve the likelihood of an opportunity being taken advantage of. Recommended actions are suggested to bring the weak area noted in the findings into line with all the relevant criteria used to determine the potential risks/implications. The internal audit recommendations should be recorded in the report, whether management has agreed to implement the recommendations or not.

In paragraph format, indicate the recommended action required for the respective finding raised (weakness identified). State the standards, measures, expectations or best practices used in making an evaluation and/or verification (what should exist). The measuring standard, against which we are measuring, should be noted in detail.

Management comments and Action Plans
A summary of the comments made by the Senior Manager / Manager in response to the sections above is recorded in this section. This gives management a chance to communicate;
- any compensating controls that reduce the negative effect of the finding;
- their agreement with the recommendations; and/or
- their undertaking to act either upon or reject the recommendations made by the internal auditor.

It is always preferable that, through effective communication, management agrees with the internal audit findings, sees value in the recommendation and undertakes to implement the recommended corrective actions.

In order to assure effective corrective action (through the direct and appropriate apportionment of responsibility and accountability) agreed management action should adhere to the following basic criteria:

- **What** – The auditor together with the client should agree to constructive corrective actions (e.g. practical, economical, efficient, etc.) that should suggest approaches for correcting the root cause/s and enhancing performance. The benefits of the implementation of the proposed action should be clearly stated and explained. The responsibility for ensuring that management responses are adequate lies with internal audit. An inadequate and /or vague management response undermines one of the objectives of the audit report, which is to ensure that effective and efficient internal and accounting controls and procedures are in place and operational at all times.

- **How** – The action plan must very clearly and very briefly explain the exact detail of the proposed action to rectify the reported weaknesses (deficiencies).

Responsible Person

The response must clearly designate responsibility to the person who will carry out and implement the required action. Management has the responsibility of ensuring that the task is clearly and timeously given to the relevant member/s of staff. If management agrees to the actions but the actions are beyond their boundaries, then the issue needs to be taken up by management with another party.

Implementation Date

The report must clearly indicate by when (date and or length of time required) corrective action will be in place.

Final Reports

This section contains a copy of the final report issued to management after the completion of the audit.

The final report must only be issued to management by the Manager: Internal Audit after he has satisfied himself as to;
- the proper completion of the planned internal audit work;
- the complete review and approval of the internal audit working papers;
- the proper clearing of all queries and items requiring follow-up after the end of the field work and the review by the Project Manager;
- whether the report meets the assurance requirements of the Audit Committee and "adds value" to management; and
- the discussion and agreement of the report with client management.

A signed copy of the final audit report must be kept in the audit working papers file under the relevant section. The only exception to this will be in a situation where the project is to investigate fraud and/or embezzlement and the perpetrators and full extent of the fraud is unknown. In these cases the report will only be submitted to the Head of the Division being audited.

3.4 FOLLOW UP

The reporting process of our audit process is followed by the follow up process, which seeks to ensure the implementation of the recommendations or action plans agreed to by the business managers. Follow up is a process of verifying if the action plans were indeed implemented over an agreed period of time. The internal audit manager/specialist performs a follow up review using the final report as a basis. Follow up review is undertaken after one hundred and twenty (120) days and/or as directed by the Audit Committee in areas of concern and/or in the event that the Manager Internal Audit considered necessary given risk areas. Furthermore, an earlier follow up may take place at the request of the Municipal Manager.

Follow up reviews, may extend to the testing of the controls implemented to determine the effectives of such controls.

Follow up reports are produced separately, however the initial report (control issues log) is set to be updated after every follow up review and where proactively the client has communicated. Upon a second review of the area, a repeat findings log is produced and reported to the Audit Committee.

Where the sought controls are not implemented, business managers are required to provide a reason for the failed or delayed implementation as well as the additional time it will take to implement such actions.
The reporting process is the same as the one detailed above, except that we indicate clearly in the RAF's if the finding is a repeat finding.

4. GENERAL
Once the audit report has been finalized, all audit files (permanent and current) should be labelled. A CD containing the electronic audit file and clearly labelled should be affixed to the current file. An audit checklist should be completed by the Auditor and reviewed by the Assistant Manager Internal Audit.
To preserve a finalized project file and protect it, the Assistant Manager Internal Audit should update the project library to indicate that an audit project has been finalized. The project file is finalised when as a minimum the following exists:
• Audit Procedures are signed off as prepared and/or reviewed;

- Work papers are signed off as prepared and/or reviewed;
- Record of Audit Findings are signed off as prepared and/or reviewed;
- Review notes are addressed and cleared;
- Related time sheets have been completed; and
- Performance Evaluation forms for the specific project have been completed.

Two files are at minimum produced at the end of each audit, namely, permanent file and project file.

Permanent File

The permanent file is prepared for each directorate being audited. This file should amongst other things contain the following information:
- Organisational Chart and Structure;
- Strategy Documents;
- Business Plan;
- Policy Manuals;
- Systems Narratives/ Descriptions;
- Risk Matrices; and

Management review/Supervision

All audit working papers should be reviewed to ensure that they properly support the audit report and that all necessary auditing procedures have been satisfactorily performed.

The review of working papers is performed by the Assistant Manager Internal Audit. The following issues should be considered when reviewing internal audit working papers:

- Has all planned audit work been performed as intended?
- Has all audit work been properly performed and documented?
- Does the work performed satisfactorily meet the present audit objectives?
- Do working papers support the conclusions reached?
- Are findings and conclusions clearly stated?
- Does the report "Add value" to the client and meet their expectations?
- Are all working papers that should be present actually filed as evidence?
- Are there any unnecessary working papers on the file?

The reviewer usually writes review notes or questions arising from the review process. These queries/notes should be kept in this section of the file, during the course of the audit.

All review notes must be removed from the audit file once the Manager Internal Audit is satisfied that queries have been satisfactorily cleared and details included in the audit working papers.

The review queries/notes are addressed and cleared by the preparer of the work by ensuring that the working papers provide adequate evidence that questions raised during the review have been resolved.

The preparer of the work must also indicate on the review notes that all questions raised have been cleared. The review note is "cleared" when the Assistant Manager Internal Audit is satisfied that an appropriate answer to his/her query is clearly recorded in the internal audit file (preferably on the relevant audit working papers, rather than on the query sheet) and properly constitutes audit evidence.

Evidence of supervisory review should consist of the reviewer initialling and dating each working paper after it is reviewed."

After the detailed review of audit working papers, it is necessary for the reviewer "to take a step back and then assess whether during the audit all critical risks have been identified and adequately dealt with".

Audit Completion
The purpose of this section is to provide a record of the steps taken by the audit team and the Project Manager to ensure that the audit was completed according to the approved standards.

- **Audit Completion Summary**
A standard checklist - the "Audit Completion Summary" - is to be completed and placed on file 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" consists of a series of areas for consideration upon finalisation of the audit.

The "Audit Completion Checklist" is to be signed off by both the Auditor and the Manager Internal Audit. If they are both satisfied that the audit process/step under consideration has been properly performed and documented, they should initial the audit completion summary and include the working paper reference of where the performance of the work step is evidenced, where appropriate.

All the areas listed on the audit completion summary must be specifically addressed. Where no specific working papers are on file to evidence the proper performance of a process/step, separate notes should be attached to the audit completion summary providing the necessary details and conclusions.

5. AUDIT LIAISON AND AUDIT COMMITTEE REPORTING

The information contained in the final report (table on all findings) will be used for reporting to Audit Committee on the adequacy of risk management, internal control and governance processes.

6. CONCLUSION

This document will be reviewed annually to address any developments in the Internal Audit Profession and ULMIAU. Any changes to this document shall be effected through the Audit Committee and approved by the Manager: Internal Audit.