

Reference: T8/2/31

## **TREASURY CIRCULAR MUN NO 45 of 2014**

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THE MAYOR, MOSSEL BAY MUNICIPALITY: MS M FERREIRA  
THE MAYOR, GEORGE MUNICIPALITY: MR C STANDERS  
THE MAYOR, OUDTSHOORN MUNICIPALITY: MR G APRIL  
THE MAYOR, BITOU MUNICIPALITY: MR M BOOYSEN  
THE MAYOR, KNYSNA MUNICIPALITY: MS J WOLMARANS  
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THE HEAD: BRANCH GOVERNANCE AND ASSET MANAGEMENT (MR Z HOOSAIN)  
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THE PROVINCIAL AUDITOR

MASTER RECORDS OFFICIAL: BUSINESS INFORMATION AND DATA MANAGEMENT

THE HEAD OF DEPARTMENT: LOCAL GOVERNMENT

THE CHIEF DIRECTOR: LOCAL GOVERNMENT BUDGET ANALYSIS – NATIONAL TREASURY (MR J HATTINGH)

THE CHIEF DIRECTOR: MFMA IMPLEMENTATION – NATIONAL TREASURY (MR TV PILLAY)

# THE ROLE OF INTERNAL AUDIT AND THE AUDIT COMMITTEE IN COMBINED ASSURANCE

## 1. PURPOSE

To disseminate guidance on the role of internal audit and the audit committee in combined assurance.

## 2. BACKGROUND

Provincial Treasury issued a framework on combined assurance in June 2012 via PT Circular Mun 29 of 2012. Minimal progress has since been noted on the implementation of Combined Assurance.

PT has therefore extracted, from the IIA Standards and other guidance sources, the roles of internal audit and the audit committee in combined assurance that can be practised whilst enterprise risk management is developing.

## 3. WAY FORWARD

Please relay to the internal audit activity and audit committee. Audit committees are to heed the roles of the internal audit activity in combined assurance and oversee the practice thereof.

The application of the audit committee roles in combined assurance should be added to the performance evaluations.

Provincial Treasury will also verify the application of the respective roles in combined assurance during the MGRO process.



**B VINK**

**SENIOR MANAGER: FINANCIAL GOVERNANCE**

**DATE:** 5 September 2014



**Western Cape  
Government**

Provincial Treasury

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# **The Role of Internal Audit and the Audit Committee in Combined Assurance**

September 2014

## Introduction

Since the release of King III in 2009, the concept of Combined Assurance was spurred into action. Frameworks sprouting from both the private and public sector were introduced as a basis for the implementation in this unchartered water.

Five years down the line, the reasoning for Combined Assurance and terms such as "three lines of defence" are understood. Why then, has Combined Assurance not moved from the framework to application?

A step in the right direction will be to explore the roles of the internal audit activity and audit committee in combined assurance.

## Internal Audit in Combined Assurance

Internal Standards for the Professional Practice of Internal Auditing (ISPPA) and its associate Practice Advisories (PA) state that *The chief audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimise duplication of efforts.*

### Role 1: Internal Audit an Assurance Provider<sup>1</sup>

The Chief Audit Executive (CAE) should ensure that the internal audit charter / engagement letter specifies that the internal audit activity has access to the work of other internal and external assurance providers.

The internal audit activity (IAA) will provide assurance over the entire organisation. This should include:

- assurance on the design and adequacy of the risk management processes;
- management of the top risks including the effectiveness of the controls and other responses;
- verification of the reliability and appropriateness of the risk assessment and reporting of the risk and control status.

With the assurance map of the organisation as a basis, the internal audit activity should consider areas of inadequate coverage when developing the internal audit plan.

In instances that the CAE is hiring an assurance provider, the CAE should document engagement expectations in a contract or agreement. The following minimum expectations should be set to ensure that work is adequate and reporting requirements are fulfilled:

- the nature and ownership of deliverables,
- methods / techniques,

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<sup>1</sup> Practice Advisory 2050-3

- the nature of procedures and data / information to be used,
- progress reports / supervision

IA then considers the following to conclude whether to rely on the work of the assurance provider:

- independence and objectivity
- competencies and qualifications
  - eg verifying appropriate professional experience and qualifications
  - current registration with relevant professional body or institute
  - reputation for competency and integrity in the sector
- elements of practice to have reasonable assurance that the findings are based on sufficient, reliable, relevant and useful information<sup>2</sup>
- the work of the assurance provider is appropriately planned, supervised, documented and reviewed

The internal auditor should be satisfied that the findings appear to be reasonable, based on knowledge of the business, environment, techniques and information used by the other assurance provider

If management within the organisation contracts a third-party assurance provider, within the combined assurance framework, the internal auditor should be satisfied that the instruction is appropriate, understood and executed.

When organisations require an overall opinion from the CAE, the CAE should understand the nature, scope and extent of the integrated assurance map to consider the work of other assurance providers, rely on it as appropriate, before presenting an overall opinion on the municipality's governance, risk and control processes. The IA should include reference to other assurance providers where reports rely on such information.

Instances where the municipality does not expect an overall opinion, the CAE can act as the coordinator of assurance providers. The CAE should report on any lack of input by other assurance providers. If the CAE believes that the assurance is inadequate or ineffective, the Municipal Manager and Audit Committee should be advised accordingly.

The IAA should follow up on recommendations made by other assurance providers and should determine whether management has implemented the recommendations or accepted the risk of not taking action.

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<sup>2</sup> Refer to Standard 2310

## **Role 2: The CAE is responsible for coordinating internal and external audit work<sup>3</sup>**

It is important that the CAE obtain the support of the audit committee to coordinate audit work effectively.

It should become common practice that internal and external audit rely on the work of the other to increase efficiencies. In this case, sufficient information should be provided to enable the other party to understand the techniques, methods and terminology to facilitate reliance on the work performed.

*Planned audit activities of internal and external auditors need to be discussed to ensure that audit coverage is coordinated and duplicate efforts are minimised where possible. Sufficient meetings are to be scheduled during the audit process to ensure coordination of audit work and efficient and timely completion of audit activities and to determine whether observations and recommendations from work performed to date require that the scope of planned work be adjusted.*

Whatever comes to light from the external audit management letters should be understood by the CAE and used as input to planning the areas to emphasize in future internal audit work.

The CAE should also ensure that appropriate follow-up and corrective action has been taken by senior management on matters raised in the management letters.

The CAE is responsible for regular evaluations of the coordination between internal and external audit. The CAE then communicates the results of these evaluations to the MM and AC.

### **The Audit Committee in Combined Assurance**

The role of the AC in combined assurance is two-fold:

1. An assurance provider, giving independent and objective assurance
2. Ensuring that a combined assurance model is applied that will provide a coordinated approach to all assurance activities

The AC is an independent committee responsible for the oversight of control, governance and risk management. The AC should provide independent and objective view of the municipality's risk management effectiveness. In so doing, the AC is verifying risk mitigation and internal and control which, by definition is providing assurance.

Responsibilities of the AC include:

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<sup>3</sup> Practice Advisory 2050-1

- reviewing and recommending disclosures on risk in the annual report
- providing feedback on the adequacy and effectiveness of risk management
- ensuring internal and external audit plans are aligned to the municipality's risk profile
- satisfying itself that financial reporting risks, internal financial control and information technology risks are appropriately addressed

The audit committee is supported by internal audit, external audit and other credible assurance providers when providing independent and objective assurance. It is the AC however that is required to disclose annually to all stakeholders. The AC report includes reference to compliance with the municipality's statutory duties, the independence of external audit, the view on the financial statements and accounting practices and whether internal financial controls have been effective. As an assurance provider, the AC is reporting on specific areas of risk within their domain.

### **Role 2: Ensuring that a Combined Assurance Model is Applied<sup>4</sup>**

The audit committee should ensure that a combined assurance model is applied to provide a coordinated approach to all assurance activities

This role emanates in the following primary tasks:

- The AC should ensure that the responsibilities for combined assurance are appropriately reflected in the AC Charter
- The AC should encourage cooperation between internal and external audit
- The AC should review coverage and scope between internal and external audit to avoid duplication and allow for possible cost savings from the integration of the two functions. Timing of internal audits and the months during the financial period that the audit scope will cover must be aligned.
- The AC should review, provide input and adopt the Combined Assurance Plan (CAP)
- Ensure that the CAP can be clearly linked to the risk assessment
- Ensure that all high risk areas are included in the plan
- Review quarterly reports that reflect actual performance by the different assurance providers and compare with the CAP
- Review corrective action taken when identified risks are not being covered by assurance activities

Importantly, the AC should measure the extent to which they were able to fulfil their combined assurance responsibilities and appropriately report on this in their annual report.

### **Conclusion**

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<sup>4</sup> King III, 3.5



The risk registers are a primary source of information when compiling the combined assurance plan. The application of combined assurance should ensure that all strategic risks and significant risks are properly mitigated and covered by assurance providers. For combined assurance to succeed, enterprise risk management must be operating effectively.

Should this not be the case, the role of internal audit and the committee in the combined assurance plan, begins with *the evaluation of the effectiveness of risk management and their contributions to the improvement of risk management processes*<sup>5</sup>.

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<sup>5</sup> Standard 2120