



Developing of a framework to evaluate the internal audit functions at municipalities in South Africa

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ABSTRACT

This research examines internal audit functions (IAFs) in municipalities in South Africa. Municipalities are established to provide services to the people residing within them, and do so by providing various services such as water and electricity supply, sanitation, roads, etc. It is therefore important for every IAF within municipalities to continuously evaluate their operational plans and best practice business processes to ensure that citizens' expectations are met.

The Auditor-General South Africa (AGSA) continues to express concern about the quality of financial governance in municipalities, as evidenced by the adverse audit opinions issued annually by the auditor-general's office. This research therefore intends to contribute to the existing body of academic knowledge by pursuing the following objectives: developing a practical framework to effectively add value to municipalities by facilitating their IAFs; identifying the roles and responsibilities of IAFs within municipalities; identifying the challenges that prevent the smooth functioning of IAFs in municipalities; considering and discussing what must be done to ensure that the internal audits are independent; identifying the characteristics of effective IAFs for South African municipalities.

To achieve the research objectives, a non-positivist paradigm or constructivist paradigm was applied for objectivity, reliability, and in support of generalisation. The study followed a qualitative and sequential explanatory design to achieve the stated objectives. Data was collected from the auditor-general's consolidated municipal reports from all existing South African municipalities as at 31 December 2017. It was then condensed to concepts that described the research phenomenon. The research was limited to the use of municipal audit reports for all the municipalities in each of the three types of municipalities, over a period of five years. Using a content analysis approach, 30 auditor-general reports were examined for each of the five years between 2011/2012 – 2015/2016. This produced a set of 150 reports for analysis.

Atlas.ti software was used to analyse these reports and the results were translated to develop the framework suggested by this study. Results of the analyses revealed that the IAFs within many South African municipalities do not fulfil their responsibilities, leading to these municipalities obtaining qualified audit opinions, disclaimer opinions, and claims of mismanagement of resources. The lack of progress within the municipalities was often found to be due to inadequate oversight of the IAF, which was not always fully capacitated with skilled, experienced staff trained to perform the necessary oversight. It is apparent that in many municipalities, IAFs do not contribute positively to the audit outcomes, and that senior management fails to take these functions seriously, resulting

in the same audit opinions and findings by the Auditor-General South Africa (AGSA) year after year.

Findings from the analysis corroborated those found in the literature, thus confirming the four stated research objectives. From this analysis, the researcher developed a framework for an effective IAF for municipalities in South Africa. The framework was developed based on the literature gathered, the key findings obtained from the audit reports and the recommendations made by AGSA. This framework contributes to the current body of knowledge on the topic, and constitutes the achievement of the primary objective of the research.

Keywords:

District municipalities, effectiveness, independence, internal audit functions, internal audit unit, metropolitan municipalities, municipalities, local municipalities, roles and responsibilities, stakeholders, value adding.

DEDICATION

I dedicate this thesis to my late mother Mahlabirwa Magriet Mankge-Mamaile for her inspiration and support since my early age until I obtained my degree. Rest in peace my mom; you will remain special to me and my future generations.

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LIST OF ACRONYMS

AAT (SA)	Accounting Technicians South Africa
AC	Audit Committee
AGSA	Auditor-General South Africa
AICPA	American Institute of Certified Public Accountants
AO	Accounting Officer
BSC	Balanced Scorecard
CAC	Chairpersons of Audit Committees
CAE	Chief Audit Executive
CBOK	Common Body of Knowledge
CPD	Continuous Professional Development
CFO	Chief Financial Officer
CIA	Certified Internal Auditor
CEO	Chief Executive Officer
COGTA	Department of Cooperative Governance and Traditional Affairs
COSO	The Committee of Sponsoring Organisations of the Treadway Commission
DMA	District Management Areas
ERM	ERM - Enterprise Risk Management
GAO	General Accounting Office
GIA	General Internal Auditor
GRAP	Generally Recognised Accounting Practice
HOD	Head of Department
IA	Internal auditor
IAF	IAF
IFAC	International Federation of Accountants

IIA	Institute of Internal Auditors
IIASA	Institute of Internal Auditors South Africa
IIASPPI	Institute of Internal Auditors' Standards for the Professional Practice
INTOSA	International Standards of Supreme Audit Institutions
IPPF	International Professional Practices Framework
ISPPIA	International Standards for the Professional Practice of Internal Auditing
ISSAI	International Standards of Supreme Audit Institutions
KPI	Key Performance Indicators
MEC	Member of Executive Council
MFMA	Municipal Finance Management Act
MPAC	Municipal Public Accounts Committee
MSA	Municipal Structures Act
OCA	Operation Clean Audit
PAA	Public Audit Act
PCC	President's Coordinating Council
PFMA	Public Finance Management Act
ROI	Return on Investment
SALGA	South African Local Government Association
SOX	Sarbanes-Oxley Act
VFM	Value-for money

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CHAPTER 1

INTRODUCTION AND STUDY BACKGROUND

1.1 INTRODUCTION

Report III by the Institute of Internal Auditors (IIA) Global Internal Audit Survey on measuring the value of internal auditing (2011: 2), suggests that the “basic concept of the internal audit function (IAF) is that its value is determined by its usefulness to its organisation”. The usefulness of IAFs and services is reflected through its perceived contribution to its stakeholders. The question that therefore arises is whether the IAFs at municipalities in South Africa are perceived by stakeholders as adding value, and if these services can be regarded as useful to them.

The IAF is regarded as effective if it meets the intended outcome it is supposed to bring about (Mihret & Yismaw, 2007: 1). This statement became the cornerstone of this research, as the study intended to establish if the IAFs within the municipalities in South Africa are effective, and if so, to what extent. The main objective of the study was to develop an effective framework to assist these municipalities by adding the required value that was found to be absent. Sawyer (1995:231) stated: “...the internal auditor's job is not done until the identified weaknesses are corrected and remain corrected”. Van Gansberghe (2005: 12) supported this statement by indicating that internal audit effectiveness in the public sector should be evaluated by the extent to which it contributes to effective and efficient service delivery, as this drives the demand for improved internal audit services.

IAFs are undoubtedly expected to play an important role in all the organisations, both private and public sector organisations, by assisting those in management to improve performance and accomplish their goals, thus adding value to their organisations. The IIA, through the International Professional Practices Framework (IPPF), provides the standards that guide internal auditors on their expected roles and how these standards assist them in serving their organisations to the best of their abilities.

Gramling, Maletta, Schneider, and Church (2004: 197) stated that those in authority within the organisation sets the overall tone for governance within an organisation and create the atmosphere that will allow the goals and objectives to be achieved. The IAF, on the other hand, is expected to interact with management by providing evaluations of the organisation's systems of internal control. The IAF through the management support and recognition of the IAF, can perform their activities in accordance with set standards, and assist those in authority to accomplish the organisation's objectives. The IAF should have a strong standing in an organisation and must be recognised as a core part of governance, not as some form of necessary burden or add-on. In

addition, McKay (2006:18) stated that the IAF is an important component of a government agency's internal control structure and environment. This emphasises the indisputable importance of the IAF within an organisation. However, the available literature shows that IAFs in South Africa lack the necessary influence to be effective, hence the need for a framework to guide them to their full effectiveness (Auditor-General South Africa, 2011:32; Auditor-General South Africa, 2012:86; Auditor-General South Africa, 2013:31).

Ahmad, Othman, Jusoff, et al. (2009), directly linked the independence of IAFs to their effectiveness by stating that IAFs are effective only if they are independent. This view is supported and maintained by professional standards worldwide, such as the guidelines of the International Standards for the Professional Practice of Internal Auditing (ISPPIA), and the IIA Practice Advisory. The latter suggests that the independence of an IAF can be gained by means of: reporting to levels within the organisation that allow the IAF to perform its responsibilities freely from interference; circumventing conflicts of interest; having direct contact with the board and senior management; having unrestricted access to records, employees and departments; the appointment or removal of the head of internal audit function not being under the direct control of the executive management; and not having to perform non-audit work.

1.2 PROBLEM STATEMENT

The regulation by the Municipal Finance Management Act No.56 of 2003 (MFMA), regarding IAFs, states that IAFs should prepare an audit plan that is risk-based and an internal audit programme for each financial year, and advise the organisation's accounting officers accordingly. The MFMA further outlines what the audit committees should do within the municipalities with regard to the implementation of internal audit plans and matters relating to internal audits; internal controls; accounting procedures and practices; risk and risk management; performance management; and loss of control and compliance with this Act (MFMA, s165). However, the AGSA continues to express concern about the quality of financial governance, as evidenced by the adverse audit opinions issued by the AGSA annually (Auditor-General South Africa, 2011:32; Auditor-General South Africa, 2012:86; Auditor-General South Africa, 2013:31, 35, 75, 103; Auditor-General South Africa, 2014:34, 39, 79, 109). The AGSA specifically states that IAFs in municipalities do not adequately evaluate internal controls, and therefore do not fully advise or report to the audit committee on matters such as accounting, risk management and loss control (Auditor-General South Africa, 2011: 32; Auditor-General South Africa, 2012: 86; Auditor-General South Africa, 2013: 31, 35, 75, 103).

According to Africacheck, about 30 service delivery protests are experienced in South Africa every day, (Bhardwaj, 2016) while these statistics were contested by some political parties, the Municipal

IQ has recorded 164 service delivery protests in 2017 in South Africa. All these protests were found to be related to service delivery (www.municipaliq.co.za). All these protests are directed towards municipalities in South Africa and these municipalities have IAFs in place to assist among others those in authority in carrying out their functions. This poses a question of what are the challenges faced by the municipalities despite having the IAFs? This is further supported by the study conducted by Pillay (2016:2) that states that corruption occurs more readily where there is systematic and organisational encouragement for someone to become corrupt, raising the question: where are IAFs in this situation?

As previously stated, according to the MFMA and the IIA, IAFs should assist in advising accounting officers, among others, on points such as internal controls, accounting procedures to improve financial practice and performance, risk areas and management of such risks, performance management, and compliance with the appropriate laws. It is therefore evident that IAFs in South African municipalities are not effective, as these municipalities continue to annually receive disclaimers and adverse opinions from the AGSA despite having IAFs in place. The problem is that there is no specific framework in place to guide IAFs on how to function and assist this sphere of government in order to ensure that they remain effective and add value to their organisations while remaining independent, as required by the legislation.

1.3 OBJECTIVES OF THE STUDY

The following objectives were formulated for the study:

1.3.1 Primary objective

This study intended to develop a practical framework for IAFs to effectively add value to their municipalities in South Africa, therefore, becoming effective.

1.3.2 Theoretical objectives

In order to achieve the primary objective, the following theoretical objectives were formulated for the study:

(1) to identify the roles and responsibilities of an IAF within a municipality; (2) to identify the challenges that prevent the smooth functioning of the IAFs in South African municipalities; (3) to discuss what must be considered in order to ensure the independence of an IAF; (4) to identify the characteristics of an effective IAF.

1.3.3 Empirical objectives

In accordance with the primary objective of the study, the following empirical objectives were formulated:

(1) to analyse the AGSA reports with the aim of determining the key findings leading to disclaimers and adverse opinions within municipalities in South Africa; (2) to analyse the AGSA reports to determine the independence of the IAFs in South African municipalities; (3) to develop a framework for an effective IAF in South Africa.

1.4 RESEARCH DESIGN AND METHODOLOGY

The study followed a qualitative sequential explanatory design, with analysis of the collected qualitative data done through content analysis, in order to develop a practical framework for an effective IAF. Qualitative content analysis is one of the numerous qualitative methods available for analysing data and interpreting its meaning (Schreier, 2012), and was used in the study to analyse and interpret the AGSA municipality reports. Qualitative content analysis “is a research method that embodies a systematic and objective means of describing and quantifying phenomena” (Downe-Wamboldt, 1992; Schreier, 2012). As a fundamental requirement for a successful content analysis, data is condensed into concepts that describe the research phenomenon (Hsieh & Shannon, 2005) by creating categories, concepts, a framework, and a conceptual system or conceptual map (Weber, 1990).

This qualitative content analysis utilised an inductive content analysis approach, which involved three main phases: preparation, organisation and reporting of results. The preparation phase consisted of collecting suitable data from the AGSA reports for content analysis, making sense of the data, and selecting the unit of analysis. “The organisation phase included open coding, creating categories, and abstraction” (Elo & Kyngäs, 2008). The reporting phase included “a description of the content of the categories that described the phenomenon by using an inductive approach”. Atlas.ti was used to analyse the data obtained from the AGSA reports. This covered a period of five years (being the AGSA reports from 2011/2012 to 2015/2016), which provided sufficient information to determine and analyse a number of factors necessary for this study. The content analysis of AGSA audit reports focused on the following:

- The type of audit opinions provided to municipalities in South Africa for the period 2011/2012 to 2015/2016;
- Characteristics of an effective IAF;
- Role and responsibilities of an IAF within a municipality;
- Independence of the IAFs as evaluated by AGSA;

- Comments made by the AGSA on the municipalities' IAFs in South Africa;
- Major weaknesses found by the AGSA on municipalities' IAFs;
- Recommendations by the AGSA on how IAFs can improve their functioning; and
- Trends of IAFs from 2011/2012 to 2015/2016 in terms of improvement.

This methodology provided the basis or foundation for the development of the framework for this study.

1.5 EMPIRICAL STUDY

The empirical portion of this study comprised the following methodological dimensions:

1.5.1 Target population

As indicated, the study followed an exploratory sequential approach, meaning that the population of the study consisted of the 285 AGSA reports provided to the 285 municipalities existing in South Africa, as at 31 December 2017. Therefore, the empirical data was collected by sampling these reports. The target population therefore, was the AGSA municipalities' reports from 2011/2012 to 2015/2016, covering a period of five years. This provided sufficient data to make an informed conclusion.

1.5.2 Sample size

In the first phase, the sample size comprised 10% of the 285 AGSA municipalities' reports, being equal to 30 reports multiplied by five years, amounting to 150 reports analysed for the study. These sampled AGSA reports were stratified to the three main types of municipalities' existing in South Africa: namely, type A, B, and C municipalities. The researcher divided the municipalities into three distinct strata and randomly selected reports for analysis from each group. Sampling was done by randomly taking five reports from type "A" municipalities (out of a possible eight reports), 10 reports randomly selected from type C municipalities (out of a possible 47 reports) and 15 reports randomly selected from type B municipalities (out of a possible 230 reports).

The study's sample sizes were in line with those used by similar studies conducted in other countries. For instance, in a study by Shewamene (2014) on the determinants of internal audit effectiveness in the public sector in Ethiopia, (a case study on selected Ethiopian public sector offices), a sample size of 72 participants was targeted and used. Therefore, the sample size of this study was appropriate and enabled the researcher to generalise the findings to all other South African municipalities that were not selected for analysis.

1.5.3 Sampling method

The random sampling method that was used to stratify the municipalities' reports into subgroups, ensured that every municipality in each group had an equal chance of being selected, and that municipalities were selected without bias. This type of sampling was appropriate for the study as it provided the results without any element of bias.

1.6 STUDY APPROACH AND DATA COLLECTION METHOD

1.6.1 Data collection method

Content analysis is defined as “a systematic, replicable technique for compressing many words of text into concise content categories, based on the explicit rules of coding” (Krippendorff, 1980; Weber, 1990). Krippendorff (1980) offered a comprehensive definition of content analysis as: “any technique for making inferences by objectively and systematically identifying specified characteristics of messages”. Content analysis enables researchers “to examine large volumes of data, such as the AGSA reports in this study, with relative ease and in a systematic manner (Krippendorff, 1980). Content analysis is a useful technique for allowing researchers to discover and describe the focus of individuals, groups, institutions or of social attention (Weber, 1990)”. It also allows for possible interpretations which can be validated using other methods of data collection. Krippendorff (1980) noted that: “too much content analysis research is motivated by the search for techniques to deduce from symbolic data what would be either too costly, no longer possible, or too obtrusive by the use of other techniques”.

Content analysis is also useful for examining trends and patterns in documents, such as those analysed in this study. For example, Stemler and Bebell (1998) conducted a content analysis of school mission statements to make some inferences on what these schools held as the primary reason for their existence. One of the major research questions was whether the criteria being used to measure their program's effectiveness (e.g., academic test scores) was aligned with the overall program objectives, or with the reason for their existence. This method yielded good results from a cost-effective and reliable research method that could objectively be compared to data collected at some point in the future, in order to determine if policy changes related to standards-based reform have manifested in school mission statements.

Content analysis “has become a powerful tool lately, when compared with other research methods such as interviews, observation, and the use of archival records” (Elo & Kyngäs, 2008). It is useful for analysing historical material, especially for documenting trends over time, and thus was relevant for this study.

In comparison to other research methods, content analysis “scores highest with regard to ease of repetition. Study material of this nature is usually available for others to use” (Weber, 1990: 35), and therefore a study can be repeated, and the same results will be realised.

1.6.2 Approached followed

The study used an inductive approach as recommended by Thomas (2012). The aim of using this approach is to reduce raw written data to a brief, summary format; establish clear links between the evaluation or research objectives and the summary findings derived from the raw data; and develop a framework of the underlying structure of experiences or processes evident in the raw data (Thomas, 2012). Thomas (2012) further stated that a general inductive approach provides a systematic set of procedures for analysing qualitative data that produces reliable and valid findings. The inductive approach provides a simple, straightforward approach to derive findings in the context of focused evaluation questions. This approach was relevant for the study.

1.6.3 Statistical analysis

The following statistical methods were used for the empirical data sets:

1.6.3.1 Trustworthiness and credibility

To ensure the trustworthiness and credibility of the data collected and analysed in this study, atlas.ti software was used for testing the analysis and building the framework.

The General Inquirer classical package for content analysis studies was used in the study, supplemented by the Intext software as developed by Harald Klein (1981) for reliability and validity of analyses.

1.6.3.2 Descriptive analysis

In this study, data analysis was conducted in a three-stage process of data reduction, data display and extraction of conclusions. The collected data was analysed using the packages and software mentioned above.

1.6.3.3 Significance tests

The differences in results, due to the fact that the analysis was made from different categories of municipalities, were analysed using the analysis of variance (ANOVA). This was done to test whether capacity, resources or other factors had any impact on the results of the study.

1.7 LITERATURE REVIEW

The literature review includes secondary data sources taken from relevant textbooks, journal articles, newspaper articles and from the Internet. The available literature discusses the origin of internal audits and their value-adding role, as viewed by different sources. This section (which will be chapter 2 – 4) explains the history, development, and nature of internal auditing as a profession. This is followed by a discussion of the rules and regulations governing municipalities in South Africa. This section is followed by a discussion on views of the effectiveness of internal auditing, which indicate how different sources view the effectiveness of IAFs. The section is followed by the presentation of other research work on the effectiveness of internal auditing and the areas on which it was focused. This will be followed by a section covering all the municipalities in South Africa.

1.8 ETHICAL CONSIDERATIONS

The necessary ethical considerations were taken into account, in accordance with the North-West University rules and regulations. The Study Proposal was presented to North-West University's Ethics Committee for clearance, which was granted on the 29 May 2016.

1.9. CHAPTER CLASSIFICATION

Chapter 1: Introduction and study background

This chapter defined the research problem and outlined the aims and objectives of the study. A brief overview was given of the research design and research methods as well as a preliminary literature review.

Chapter 2: The origin of internal audit and its value-adding role

This chapter describes the origin, development and nature of the internal audit profession. The discussion of the evolution of the International Standards for the Professional Practice of Internal Auditing (ISPPA) is presented. The different roles expected to be played by the IAFs are discussed. The internal audit charter and its role within the IAF is discussed. The determination of the value added by the IAF within the organisations is discussed. The relationship between the IAFs and the audit committees is discussed. The chapter further discusses the need for IAFs at South African municipalities. The independence of the IAFs is discussed in reference to MFMA.

Chapter 3: The rules and regulations governing IAFs in South African municipalities

This chapter discusses the laws and regulations governing the practice of internal audit as a profession. And the chapter further discusses the standards applicable in IAFs including those

applicable specifically for the municipalities in South Africa. The chapter further discusses all types of municipalities found in South Africa as at 31 December 2017.

Chapter 4: The effectiveness of IAFs

This chapter looks into the effectiveness of IAFs in South Africa, as discussed in the available literature. Past and present studies conducted on the effectiveness of IAFs and their determinants are examined.

Chapter 5: Research design and methodology

This chapter provides an in-depth description of the relevant research design and methods used in the study. The achievement of validity and reliability of the results is discussed.

Chapter 6: Findings, results, and interpretation

Chapter six presents the results and analysis of the empirical study conducted. The chapter interprets the results obtained, and presents an explanation of the framework developed through the study.

Chapter 7: Conclusion and Recommendations

Based on the results of the empirical study, this chapter summarises the research results in the context of the research problem and its aims. Recommendations are made for IAFs and a framework outlining gaps in the current practice in South African municipalities, and how such gaps can be overcome.

CHAPTER 2

THE ORIGIN OF INTERNAL AUDIT AND ITS VALUE-ADDING ROLE

2.1 INTRODUCTION

As discussed earlier, the Report III issued by the Institute of Internal Auditors (IIA) Global Internal Audit Survey on measuring the internal auditing's value (2011: 2), suggests that the "basic concept of the IAF (IAF) is that the value of an IAF is determined by its usefulness to its own organisation. In this report the stakeholder perception also reflects opinion on the usefulness of internal audit services as provided by the IAFs. The question that arises is whether the IAFs at municipalities in South Africa are perceived to be adding value to stakeholders in municipalities.

The IAF is regarded to be effective if it delivers the value it is expected to bring to an organisation (Mihret & Yismaw, 2007: 1). This statement becomes the foundation for this study as it is intended to establish whether the IAFs in municipalities in South Africa are effective or not, as stated in the primary objective in Chapter 1. Sawyer (1995) states that, "... internal auditor's task is not completed until the identified weaknesses are corrected and remain corrected." Van Gansberghe (2005: 12) supports this statement by stating that the internal audit's value or effectiveness in the government sector should be assessed by the extent to which the IAF contributes to effective and efficient service delivery, as this drives the demand for improved internal audit services.

Therefore, the IAFs are expected to play a vital role in their organisations both private and public sectors in assisting those in management in accomplishing the goals set for their organisations. The IIA, through its International Professional Practices Framework (IPPF), provides standards that guide internal auditors on the role they should play to assist their organisations as to achieve their planned goals. IAFs are expected to add value in their organisations to assist in improving their performance and thereby realise their planned goals.

This chapter discusses the origins and history of internal auditing and its development as a profession. The discussion of these topics in the literature revealed that the internal audit discipline was established in 1941, and narrated the manner in which the profession evolved over the years of its existence. This information assisted in providing the necessary foundation for this research study. Topics on the adding role of IAFs and the expected roles of IAFs should play within their organisations in order for them to be considered effective were found researched in the literature.

2.2 THE ORIGIN AND HISTORY OF INTERNAL AUDITING

According to Flesher and McIntosh (2002: 1) the establishment, growth and evolution of the internal auditing profession could be directly linked with the history of The Institute of Internal Auditors (IIA), being the organisation established in 1941 in the United States to regulate the profession.

Ramamoorti (2003: 2) states that The IIA's as an organisation has existed for 75-years and its history is internationally known. According the Ramamoorti (2003: 2), the following were identified as the main contributory factors that have made the IIA what it is today:

- The formation of the international professional association devoted to the promotion and growth of the practice of internal auditing.
- The acceptance of authority, chief educator and acknowledged leader in standards, certification, research, and scientific guidance for the profession internationally.
- International headquarters for 76,400 members in 141 countries. (Flesher & McIntosh, 2002).

Ramamoorti (2003: 2) further indicates that considering the IIAs modest origins (from being a small group of 24 charter members which held the inaugural meeting in New York City on 9 December 1941), its international growth, continuing relevance, and increasing influence and recognition by the internal auditing profession over the last 75 years constitutes distinguished growth and progress. And without any doubt, the internal auditing profession certainly appears poised for continued dynamic growth and promises to become "a profession for the 21st century.

The need for both external and internal auditing originated from the necessity to have some form of independent confirmation to reduce record-keeping errors, asset misappropriation, and fraud within organisations, across all countries of the world (Ramamoorti, 2003:2). The roots of auditing as a field are defined by an accounting historian Richard Brown, as follows (1905, as quoted in Mautz & Sharaf, 1961):

"The history of auditing could be taken back to ancient times than the history of Accounting discipline. As time progresses the advance of civilisation brought about the necessity and need of one man being entrusted to some form of responsibility on the property of another man, the prudence of some kind to check upon the trustworthiness of the former was apparent".

Ramamoorti (2003: 12) in his article on internal auditing's history, titled history, evolution, and prospects, indicates that a number of historians believe that formal record-keeping can be traced as far back as 4000 BC. Historians believe that formal record-keeping systems were first introduced by business organisations and governments in the Near East, with the aim of alleviating their concerns about correctly accounting for receipts, payments and collection of taxes due. Similar growth took place in other parts of the world such as China (1122-256 BC.). The need for audits can be further traced back to public finance systems in countries such as Babylonia, Greece, the Roman Empire, the City States of Italy, etc., all of which developed comprehensive systems of accountability. Specifically, these governments were concerned with the prevention and detection of errors and inaccuracies by officials who were seen to be incompetent, as well as corrupt officials who were motivated to perpetrate fraud whenever the opportunity arose.

According to Mautz & Sharaf (1961) historians further believe that even the Bible (referring to the time period around 1800 BC/ AD. 95) "explains the basic foundation for introducing internal controls: for example, if employees have an opportunity to steal they would take advantage of it, especially if controls were non-existent. The Bible also contains examples of internal controls such as the dangers of dual custody of assets, the need for proficient and honest employees, restricted access and segregation of duties (The Bible: Colossians, 3: 23; Ecclesiastes, 9: 9-10; O'Reilly, McDonnell, Winograd, Gerson & Jaenicke, 1998). Historically then, the emergence of double-entry bookkeeping in approximately 1494 A.D. can be directly traced to the critical need for exercising stewardship and control. Throughout European history, for instance, fraud cases such as the South Sea Bubble in 18th century Britain, and the tulip scandal in Holland, provided justification for exercising more stringent controls".

The systems of bookkeeping and auditing developed in Europe were introduced into the United States due to an increase in the size, scope, and complexity in businesses. The need for separate internal assurance agencies was no longer a choice but a necessity. Independent internal assurance mechanisms were required in order to confirm important accounting information for the purpose of the company decision-makers. As time advanced, some means of assessing not only the efficiency of the work performed but also the trustworthiness of the employees were further required by the business managers. Around the mid-20th century, the formation of formal IAFs emerged, to which the responsibilities identified above were given to these IAFs. In due course, the IAFs became responsible for the "careful collection and interpretive reporting of selected business information to assist managers in keeping track of important business developments, activities, and results from diverse and voluminous transactions" (Ramamoorti, 2003: 12).

The value of the IAF was then recognised and accepted by companies in different fields such as the railroad, defence, and retail industries in the United States. These companies went far beyond financial statement auditing, and were keen to supply even the reliable operating reports containing non-financial data such as number of parts in short supply, adherence to schedules, and quality of the product (Whittington & Pany, 1998). Additionally, the General Accounting Office (GAO) of United States of America and many other State Auditors' Offices, such as the State of Ohio Auditors' Office, started to employ a large numbers of internal auditors. In summary, the collective effect of growing transaction complexity and volume, company executives' remoteness from the source of transactions, and the possible bias in reporting parties' technical accounting expertise, required businesses to review and summarise their activities in a meaningful and independent way. There was a need for organisational status to ensure that independence and objectivity are increased, and that procedural disciplines necessary for being the "eyes and ears" of management were introduced. This all contributed to the creation of an IAF within business organisations, which started as an internal business function primarily focused on protecting payroll against possible fraud, and loss of cash and other assets. The IAFs' scope quickly extended to the confirmation of almost all financial transactions and later, gradually moved from an "audit for management" emphasis to an "audit of management" approach (Reeve, 1986).

According to Moeller and Witt (1999), "the very same need for accountability and the formation of an independent assurance mechanism gave rise to the formation of internal auditing, and made it an integral part of modern business". The Institute of Internal Auditors was then established because of the growth in belief among the internal auditors that an organisation was needed in the American business structure to develop the true professional status of internal auditing. Although the internal auditing roots were in accountancy, its key purpose lied in the area of management control.

In 1941, the Institute of Internal Auditors was formally established in United States. At the beginning after its establishment, internal auditing was still seen as a closely related to the work of external auditors. During this period of early establishment internal auditors were often called upon to help external auditors in performance of financial statement reviews or accounting-related functions such as bank reconciliations. Internal auditors were perceived to be playing a fairly uncertain role within organisations and were given a limited responsibility in the total managerial spectrum (Moeller & Witt, 1999). Almost two decades after the founding of the Institute of Internal Auditors, the following definition of internal auditing, laying the ground for an operational auditing orientation, was presented by IIA (IIA, 2004:8):

“Internal auditing is an independent, objective assurance and consulting services designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes”.

The professional standards and professional responsibilities of internal auditing as a profession were formulated and pioneered by the two most influential individuals in the IIA’s history, namely Victor Z. Brink and Lawrence B. Sawyer. As a result, Victor Z. Brink was the IIA’s first research director who became active in formulating the IIA’s Statement of Responsibilities of the Internal Auditor, which was issued in 1947. This Statement then gave clarification that while internal auditing mainly dealt with accounting and financial issues, issues of an operational nature were also identified as part of its scope. In 1957, the Statement of Responsibilities of Internal Auditing had been significantly extended to include numerous services to management, such as:

1. “Evaluating and assessing the reliability, adequacy and application of accounting, financial, and operating controls.
2. Establishing the extent of compliance with established policies, plans, and procedures.
3. Establishing the extent to which company assets are accounted for and safeguarded from, losses of all kinds.
4. Establishing the reliability of accounting and other data developed within the organisation.
5. Assessing the quality of performance in carrying out assigned responsibilities”.

In 1971, being twenty-four years later after the establishment of the IIA, the chairman of the IIA’s Research Committee, Lawrence Sawyer assumed the task of effectively revising the Statement of Responsibilities. The Statement of Responsibilities experienced further revisions in 1976, 1981 and 1990 to reflect the on-going and rapid evolution of the internal auditing profession. In 1978, The IIA formally approved the Standards for the Professional Practice of Internal Auditing (Standards), which had the following purposes:

1. “Assist in communicating to others the role, scope, performance, and objectives of internal auditing.
2. Unify internal auditing throughout the world.
3. Encourage improved internal auditing.
4. Establish a basis for consistent measurement of internal auditing operations.

5. Provide a vehicle through which internal auditing can be fully recognised as a profession”.

It was evident that in 1970s already, the field of internal auditing had earned the right to be called a fully-fledged profession that was comparable to other professions and compliant with all the conditions of the profession. In 1974, the Certified Internal Auditor (CIA) examination was first sponsored by the IIA. At that point, internal auditing had a sufficiently reputable profile to merit being called an established profession. The internal auditing profession had a body of specialised knowledge (common body of knowledge was approved in 1972), a formal educational process (a minimum prescribed course of formal education), standards governing admission as a full member of the IIA (prescribed course of study, passing the CIA examination), professional experience requirements, and standards. Further, the profession had a Code of Ethics (first approved in 1968) and a recognised status indicated by a license or special designation (the CIA, or the MIIA7), which was recognised in several jurisdictions internationally. The IIA had a public interest in the work performed by its practitioners (perhaps more evident in the work performed by internal auditors in government, education, and non-profit organisations not only in the private sector), and recognition of a social responsibility.

Therefore, for the IAF to raise its organisational stature, it was important to establish a strong relationship with those charged with organisational governance who communicate directly with the audit committee. There is much evidence today that such a reporting relationship is broadly regarded as best practice in the most progressive corporations that are committed to enhancing governance structures and processes. In an early but landmark study on corporate audit committees by the Institute of Directors (IOD, 2009) it was stated:

“For the most part, the audit committee is viewed as a link between the board of directors and the auditors. To fulfil their responsibilities to shareholders and the public at large, audit committee members have had to become more interested in, and better informed on auditing matters. Management also has become aware of the necessity of protecting itself through adequate attention to internal controls and effective audits. Consequently, it has become more responsive to auditor suggestions and audit committee requests for information. (IOD, 2009)”.

By 1993, the Statement of Responsibilities of Internal Auditing noted that the scope of internal auditing includes the examination and evaluation of the adequacy and effectiveness of the organisation’s system of internal controls and the quality of performance in carrying out assigned responsibilities. At this time, the scope of internal auditing included:

1. "Reviewing the reliability and integrity of financial and operating information and the means used to identify, measure, classify, and report such information.
2. Reviewing the systems established to ensure compliance with those policies, plans, procedures, laws, and regulations that could have a significant impact on operations and reports, and determining whether the organization is in compliance.
3. Reviewing the means of safeguarding assets and, as appropriate, verifying the existence of such assets.
4. Appraising the economy and efficiency with which resources are employed.
5. Reviewing operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operations or programs are being carried out as planned".

By the early 1990s, it was well-understood that internal auditors, depending on their particular organisation's needs and preferences, "worked in several areas including compliance audits, audits of transaction cycles, investigating fraud and other irregularities, and evaluating operational efficiency. Additional areas were analysis, measurement and reporting of operational and organisation-wide risks, and other assurance and consulting activities. They performed a combination of financial reviews and audits, operational reviews and audits, management audits and compliance audits". In performing many of these activities, internal auditors made their approach risk-based and controls-focused. They also made extensive use of advanced technology applications in carrying out audits.

As time goes on the internal auditors started to display what is termed "industry specialisation" in terms of their specialised knowledge of specific industries such as health care, oil, gas and energy, defence, financial services, transportation, wholesale and retail, technology, telecommunications, media and entertainment, government and non-profits, education, etc. Internal audit staff came from diverse backgrounds, including a large proportion of non-accounting majors, and women, who gained prominence within the profession. In many cases, internal auditors became more internationally oriented, and internal auditing became rather resourceful, with internal auditors participating in and contributing to "special projects" on a contingency basis, performing the role of risk officers, ethics officers, or compliance officers, as the situation demanded". And this indicated how important the internal auditing as a profession can be within the organisations.

The discussion above provided a brief history of internal auditing from 4000 BC until the establishment of the IIA in 1941. The discussion further indicated the areas the IIA looked into from

its establishment until today. The above discussion illustrated from where the internal audit profession originated, and the approximate number of IIA members in the current era.

2.3 THE DEVELOPMENT OF THE INTERNAL AUDIT PROFESSION

According to Cascarino and Van Esch (2005: 3), the profession of internal auditing had its origins in the industrial revolution of the 19th century. At that time, the considerable growth of the business sector found existing professionals struggling to keep up with the changes of the day. Experts appeared, to cope with such radical ideas as corporate law, banking provisions and insolvencies. According to Gleim (2004a: 23), internal auditing is “a management-oriented discipline that has grown rapidly since the Second World War”. Once a function primarily concerned with financial and accounting matters, internal auditing now addresses the entire range of operating activities, and performs a correspondingly wide variety of assurance and consulting services.

“The increase in size and the decentralisation of organisations, coupled with the technological sophistication of their operations and their huge administrative and managerial complexity, could be viewed as factors that have supported the development of internal auditing and the need for an independent, objective means of evaluating and improving their risk management, control and governance processes”. Sawyer et al. (2003: 5), claim that external auditing has influenced the way in which internal auditors done their work for a number of years. Modern internal auditing had its origins in 1941 when the Institute of Internal Auditors was established, as discussed above. Only after this did internal auditors increase the scope of their work to include the evaluation of all the organisational processes. As discussed above, in the 1960s, the IIA had grown and succeeded of becoming the recognised world-wide leader of the internal auditing profession. From the time of the IIA’s establishment, it was recognised that the multidisciplinary and evolutionary nature of the business world would need to be reflected in the IIA. It had, therefore, to provide the “umbrella underneath which the individual skills and talents needed to audit the internal control mechanisms of current business could come together as equals to share knowledge and to grow”. South Africa adopted this philosophy and followed this approach with its own Chapter of the Institute of Internal Auditors.

The following section discusses the nature of internal auditing and indicates what is entailed in internal auditing.

2.4 THE NATURE OF INTERNAL AUDITING

The IIA's (2013:2) definition of internal auditing defines internal auditing as: "an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes". Goodwin (2004: 642) argues that this definition suggests that internal audit has moved away from its traditional role on financial and compliance audits to a broader value-adding role, embracing both assurance and consulting activities and focusing on improving performance and effectiveness.

The IIA (2008: 10-12) describes the IAF as:

"A critical internal assurance instrument available for public financial controls and a tool for monitoring and evaluating managerial activities prior to evaluation by external auditors. Internal auditors further ensure transparency and fairness, reduce corruption, and ensure value for money in public procurement. An IAF is an essential part of any public expenditure management system and should ensure that public spending is within budgetary provisions and that payments comply with specified procedures, as well as providing for the timely reconciliation of accounts and effective systems for management and accounting of physical and financial assets".

Therefore, the above description suggests that the internal auditors work with their organisational management to improve service delivery and ensure compliance with applicable laws, provides independent and objective assurance to an organisation's management that the identified risks are being mitigated to an acceptable level, and reports when they are not.

The IIA (2008: 10) further describes internal auditors as an integral part of government financial management and an instrument for improving performance and performance management in the public sector, who can also play an influential role in performing value-for money (VFM) audits, sometimes known as performance audits. These audits are concerned with the auditing of the economy, efficiency and effectiveness of government expenditures or spending plans. In reality, performance auditing concentrates on determining whether or not organisations are doing the right things in the best way possible.

The above discussion considered the nature of internal auditing as a discipline, which derives from its definition and which is useful in all operational areas of an organisation irrespective of the sector.

2.5 DEVELOPMENT OF INTERNAL AUDITING FUNCTION IN THE PUBLIC SECTOR IN SOUTH AFRICA

According to Van der Schyf (2000: 147), the IAFs in the public sector in the early 90s before being recognised, the IAFs mainly consisted of “internal control and inspection components, with its main efforts involved in financial and logistic inspection and compliance auditing. Valuable inputs in terms of ensuring compliance with the laws, regulations, policies, and instructions were obtained in this manner, but there were some general weaknesses”. The most prominent of these were: no specific means to test and evaluate internal controls; components relied on the third party checking function of internal control or inspection sections, reducing their own effectiveness within the department; and outputs and systems were not evaluated. These weaknesses considerably minimised the contribution of the IAF as a management tool.

As time goes on, the financial regulations were passed in terms of the Exchequer Act (Act 66 of 1975), supported by Government Gazette No. 5791 of 1 November 1996, which made it the responsibility of accounting officers to establish effective IAFs and establish an Audit Committee (Van der Schyf, 2000). It was during this period that the IAFs in the public sector were given official and statutory status in South Africa. An expectation was created that the IAF in the public sector had to move away from its traditional role of monitoring compliance with policies and procedures and reviewing financial controls, towards the modern expectation of being able to respond as a management tool to organisational and managerial needs. In 1996, momentum for the new status of South African IAFs in the public sector came from three sources:

1. The Regulations Concerning Public Entities, which were introduced in May 1993, was “an extension of the Reporting by Public Entities Act, 1992 (Act 93 of 1992), which, for the first time, made legal mention of the Institute of Internal Auditors by requiring that the IAF of public entities should function in accordance with the internal auditing standards of the Institute”. In the Regulations Concerning Public Entities (published in Government Gazette No. 5076 of 7 May 1993), which were supplementary to the Act has stated that “the board of each entity is responsible for establishing an audit committee and a functioning IAF”. Although these entities are semi-state institutions, the Act made a vital contribution in preparing the ground for statutory regulations for the establishment of the IAF in the public sector.

2. The drive for the new status of the IAF in the public sector had started in 1996, through the King I Report on corporate governance in South Africa (IOD SA, 1994). This report recommended that “all listed companies in South Africa should have an effective IAF”. This recommendation, made at the end of 1994, almost immediately created a greater awareness of the IAF in both the private and public sectors in South Africa. The recommendations regarding the IAF in the King Report were also clearly present in the provisions in Government Gazette No. 5791 of 1 November 1996, in which accounting officers were charged with the responsibility of establishing an effective IAF and an audit committee.
3. The newly-found status of the IAF in 1996 can also be linked to the influential role which the Auditor-General Act (Act 12 of 1995) played in the development of the IAF. According to section 3(4) (a)–(d), “the Auditor-General South Africa, as the independent external auditor of public sector entities, shall reasonably satisfy and ensure that reasonable precautions have been taken to safeguard the proper collection of money and that the laws and instructions relating thereto have been duly observed; reasonable precautions have been taken in connection with the receipt, custody and issue of, and accounting for, property, money, stamps, securities, equipment, stores, trust money, trust property and other assets; receipts, payments and other transactions are made in accordance with the applicable laws and instructions and are supported by adequate vouchers and that satisfactory management measures have been taken to ensure that resources are procured economically and utilised efficiently and effectively. When reporting, the Auditor-General South Africa shall in particular, mention where, in his or her opinion, the applicable internal control and management measures are inefficient or ineffective”.

The developmental history of the IAF in the public sector in South Africa was concluded with the IAF provisions, as contained in the Public Finance Management Act (Act 1 of 1999 as amended by the PFMA Act (Act 29 of 1999), and the Treasury Regulations for departments and constitutional institutions issued in terms of the PFMA Act, 1999 (Regulation Gazette No 6822 dated 31 May 2000). Section 38 of the Public Finance Management Act (PFMA, 1999) requires “the accounting officer to ensure that a national government department has an IAF, while Section 76 of the Act requires that National Treasury Regulations must promulgate what the audit committee and the IAF regulate in the national government departments. Section 3 of the Treasury Regulations provides more detailed provisions on the functioning of the audit committee and the IAF in the public sector in South Africa. The same PFMA influenced the promulgation of the MFMA, which directly regulates municipalities”.

The following section discusses internal auditing functions and the value they should add to the organisations they serve.

2.6 THE VALUE ADDING ROLE OF INTERNAL AUDITING

The International Professional Practices Framework (IPPF) defines internal auditing as “an independent, objective, assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management control and the governance process”. This definition put more emphasis on the aim of internal auditing, as to “add value” within organisations, and definition further indicates how effectiveness can be enhanced.

According to the International Standards for the Professional Practice of Internal Auditing (Standards), “add value” is defined as “the value provided by constantly improving opportunities in order to achieve organisational goals, identifying operational improvement, or decreasing risk exposure through both assurance and consulting services”. This was seen as the cornerstone for this study, which aimed to establish whether the IAFs within municipalities are effective or not, by considering what is expected from the IAF as opposed to the services the IAFs are currently providing within the municipalities. And if found ineffective, come up with the proposed framework that can be followed to ensure that the IAFs add the required value.

The IIA states that an IAF is designed to render a value-adding service to an organisation. The IPPF states that an IAF only adds value when it provides important opportunities to achieve organisational objectives, when it identifies operational improvement, and when it contributes to reducing risk exposure through both assurance and consulting services.

The concept of value-added as explained by the IIA entails among others, firstly that the IAF provides vital opportunities to achieve stated organisational objectives and goals. This means that the IAF should help the organisation in achieving its objectives, including its strategic objectives. According to a study by Melville (2003: 210), the IAF plays an active role in strategic management within organisations by evaluating and supporting the strategic management decisions made by those in authority. Ray (2009: 5) support this view, by stating that the IAF should be seen as a support function (with reference to Porter’s value chain framework), creating value within the organisation and assisting in the accomplishment of organisational objectives.

Secondly, the IAF is “expected to identify the operational improvement within an organisation. This is emphasised in the definition of internal auditing, which states that the IAFs activities should contribute to the positive improvement of an organisation’s operations (IIA, 2009). According to the IIA’s Standards, the IAF must evaluate and contribute to the improvement of, specifically, governance, risk management and control processes, systems, and operations (IIA, 2009). A wide body of knowledge exists on the contributions of IAFs to corporate governance (Sarens, 2009: 2; Archambeault, DeZoort & Holt, 2008: 376; Carcello, Hermanson & Raghunandan, 2005: 71), risk management (Fraser & Henry, 2007: 403; Sarens & De Beelde, 2006: 238; Beasley, Clune & Hermanson, 2005: 522); and control processes, systems and operations (Jeffrey, 2008: 19; Savcuk, 2007: 279–281; Zain, Subramaniam & Stewart, 2006: 4-5; Fadzil, Haron & Jantan, 2005: 849–850). Fadzil et al. (2005: 864), claimed that value-adding should be a high priority for every Chief Audit Executive (CAE), in order to influence the control of risk management and governance processes. Gramling and Hermanson (2006: 37) believed that for internal auditors, to be value-adding, they should be proactive, by taking steps to educate their board and audit committee on possible governance roles they can render.

Thirdly, the IAF should “contribute to reducing risk exposure. In order to reduce the risks identified, the IAF needs to determine what areas of difficulty may stand in the way of accomplishing the company’s stated objectives and also assess the controls that are in place to determine whether those controls are suitable and acceptable in light of the risks identified (Sawyer, Dittenhofer & Scheiner, 2003: 141-142). According to the Standards (IIA, 2009), the IAF must evaluate the adequacy and effectiveness of controls in responding to risks within the organisation’s governance, operations and information systems regarding the reliability and integrity of financial and operational information, the effectiveness and efficiency of operations, safeguarding of assets, and compliance with the laws, regulations, and contracts. De la Rosa (2007: 52) argued that IAFs are responsible for the evaluation of the accuracy of an enterprise’s risk management reporting, and should provide independent and value-adding recommendations to management. IAFs are adding value by responding to the risk impact through communication, controls, and contingencies (Pickett, 2005: 59; Hermanson, Ivancevich & Ivancevich, 2008: 14). Lastly, the definition of value-added indicates that IAFs add value by rendering both assurance and consulting services”.

According to Morse (2012: 2) a good IAF should be the “eyes and ears” of senior management, by giving honest and clear information about organisational affairs. The question is, are the IAFs within municipalities in South Africa fulfilling this function, and are they considered to be effective? Marks (2013: 1) states that “the IAF becomes effective if it provides the audit committee and executive management with the assurance they need, namely, that the organisational

management can depend on the organisation's processes and systems to manage risks towards the achievement of the organisation's objectives". This means that the IAF must provide assurance in the form of a time frame, on the current risks of the organisation.

Internal audit activities have changed from being basic administrative functions intended simply to comply with rules and regulations such as protecting company assets and issuing reports (Barac, Motubatse, Erasmus & Van Staden, 2013: 18). Independent assurances and advisory services can now add significantly more value and improve organisations' operational competencies (Arena & Azzone, 2009: 44; Morariu & Crecana 2009). These new responsibilities all support the shifting of internal auditing's efforts from the traditional role to a more advanced role that considers adding value as an important feature of an IAF.

According to Barac and Van Staden (2009: 947), this shift was further emphasised by the introduction of the Companies Act 71 (SA, 2008) which incorporated many corporate governance-related recommendations from both the King Report on Governance for South Africa, 2002 (King II) and the King Report on Governance for South Africa, 2004 (King II), that were initially included in the Corporate Laws Amendment Act of 2006. These many Acts and Reports indicate the changing role played by the IAFs, and the importance of an IAF to add value in an organisation.

Barac, Plant and Motubatse (2009: 982) supported the above discussion on the value-adding role of IAFs by stating that the IAF provides significant opportunities to accomplish organisational goals. "This implies that the IAF should assist their organisations in achieving their objectives, including the strategic objectives". A study conducted by Melville (2003: 210) found that the IAF plays an active role in strategic management within organisations by appraising and supporting the strategic management decisions made. Ray (2009: 5) argued that the IAF should be perceived as a support function (with reference to Porter's (1985) value chain framework), which creates value within an organisation and assisting in the achievement of organisational objectives.

Barac, Plant and Motubatse (2009: 983) further argued that the IAF should identify operational improvement. This is echoed in the definition of internal auditing, which highlights that the IAF's activities should contribute to the improvement of the organisation's operations (IIA, 2009). According to the Standards, the IAF must evaluate and contribute to the improvement of, specifically, governance, risk management and control processes, systems, and operations (IIA, 2009).

The above discussion considered the value-adding role of the IAF, as found in the literature. The value-adding role of the IAF is seen as crucial to the justification of its existence, and without this,

the IAF is considered useless and irrelevant. The following section looks at the role IAFs play in South African municipalities.

2.7 EXPECTED ROLES TO BE PERFORMED BY IAFS

According to the Institute of Internal Auditors (2006: 11):

“An essential element of strong public sector governance structure occurs when government auditing supports the governance roles of oversight, insight, and foresight. Because government’s success is measured primarily by its ability to deliver services successfully and carry out programs in a reasonable and appropriate manner, government audit activities should have the authority and the competency to evaluate financial and program integrity, effectiveness, and efficiency. Moreover, auditors must also protect the core values of the government, as it serves all citizens”.

The vital role played by internal auditors within organisations is evident in a study by Soh and Martinov-Bennie (2011: 611) in which they reveal that “the IAF is very important to the Audit Committee”. The study further revealed that the audit committee by itself cannot do much given that it meets after a long time, six times a year for two to three hours, working out to 18 hours annually; therefore, the audit committee needs some power, which should be provided by the internal auditors through the IAFs.

According to Chapter 7 (7.1.1) of the King IV Report, companies should establish an IAF which should perform the following functions, among others: evaluate the company’s governance processes, perform an objective assessment of the effectiveness of risk management and the internal control framework, and systematically analyse and evaluate business processes and associated controls.

The above roles/functions as stated by the King IV Code of Corporate Governance for South Africa (2016), are further supported by the IIA (2006: 13), which suggests that auditors must attempt to prevent fraud, abuse and other breaches of public trust by: assessing controls for existing or proposed functions, assessing organisational or audit-specific risks, reviewing proposed changes to existing laws, rules and implementation procedures, and reviewing contracts for potential conflicts of interest.

The Standards (1210.A3) state that internal auditors within the IAFs must, among other things have sufficient knowledge of key information technology risks and controls, and available technology-based audit techniques to perform their assigned work.

The IIA study on public sector auditing (2006: 3-12) states that there are various roles that are expected from internal auditors when performing their functions, such as oversight, detection, foresight, and insight which, if properly executed, contribute significantly to the achievement of organisational goals. These roles are discussed in the following sections.

2.7.1 Oversight role

The IIA study on public sector auditing (2006: 4), states that auditors assist decision-makers in exercising their oversight role by evaluating whether government entities are doing what they are supposed to do, spending funds for the planned purpose, and complying with applicable laws and regulations". Audits focusing on oversight must answer the following questions: Has the organisational policy been implemented as planned? and "Are those in authority implementing effective controls to reduce risks?"

The IIA study on public sector auditing (2006: 5) continues to state that the IAF supports the governance structure by verifying activities and programmes' reports of financial and programme performance, and by testing their adherence to the organisation's rules and aims. Moreover, oversight audits contribute to public accountability by providing access to this performance information to the relevant principals within and outside the organisation under audit. Both elected officials and managers are responsible for setting direction and defining organisational objectives. In addition, managers have the duty to assess risks and establish effective controls to achieve objectives and avert risks. In their oversight role, government auditors assess and report on the success of these efforts.

Oversight also describes the role of many government auditors who must detect and prevent public corruption, including fraud, inappropriate or abusive acts, and other misuse of the power and resources entrusted to government officials. Internal auditors monitor the effectiveness of management's internal control structure, to identify and reduce conditions that breed corruption. In many areas of the world, public sector auditors are also responsible for responding to allegations of corruption in the government organisations that they serve, through detection and deterrence (IIA, 2006).

2.7.2 Detection role

According to the study conducted by IIA on public sector auditing (2006: 5), detection is intended to identify improper, inefficient, illegal, fraudulent, or abusive acts that have already transpired, and to collect evidence to support decisions regarding criminal prosecutions, disciplinary actions, or other remedies. This means that the IAFs are expected to detect areas where maladministration or irregularities have taken place and clearly point them out to management to ensure that proper corrective steps are taken to avoid such activities from occurring in future.

2.7.3 Deterrence role:

According to the study conducted by IIA on public sector auditing (2006: 5), deterrence is intended to identify and reduce the conditions that lead to corruption. This means that the IAFs are expected to be proactive at all times while performing their work, and that they need to identify problematic and risky areas before such risks arise. This ensures that the organisational resources are safeguarded, and that the IAF justifies its reason for existence. It is therefore undoubtedly evident that the IAFs need to recruit the right people with specialised skills to perform this role effectively, thus adding value to the organisations concerned.

2.7.4 Insight role

According to the study conducted by IIA on public sector auditing (2006: 6), auditors provide insight to assist decision-makers by assessing which programmes and policies are working and which are not, sharing best practices and benchmarking information, and looking horizontally across government organisations and vertically between the levels of government to find opportunities to borrow, adapt, or re-engineer management practices. This role requires the auditors to be competent in their internal auditing profession, and in this case it requires the internal auditors to be well equipped with policies and have sound knowledge of this area, in order to them to add the required value. The question raised here, is whether the current internal auditors within the municipalities in South Africa able to perform this role?

2.7.5 Foresight role

According to the IIA study on public sector auditing (2006: 6), auditors also help their organisations look forward by identifying trends and bringing attention to emerging challenges before they become crises. The IAFs can highlight challenges to come, such as from demographic trends,

economic conditions, or changing security threats, and identify risks and opportunities arising from rapidly evolving science and technology, the complexities of modern society, and changes in the nature of the economy.

The Institute of Internal Auditors' article on Internal Audit Roles and Responsibilities (2006: 2) further describes the main roles and responsibilities of the IAF as: evaluate and provide reasonable assurance that risk management, control and governance systems are functioning as planned. And will enable the organisation's objectives and goals to be met; report risk management issues and internal control deficiencies identified directly to the audit committee; provide recommendations for improving the organisation's operations, in terms of both efficient and effective performance; evaluate information security and associated risk exposures; evaluate regulatory compliance programmes in consultation with legal counsel; evaluate the organisation's readiness in case of business interruption; maintain open communication with management and the audit committee; team up with other internal and external resources as appropriate; engage in continuous education and staff development; and provide support to the company's anti-fraud programmes.

The Statement of Local Government Auditor Responsibilities (2008: 11) supplemented the IAF's key responsibilities by suggesting the following responsibilities of a local government auditor as: establishing strategic and operational objectives; determining policy and making decisions; ensuring that services meet the needs of users and ratepayers and engage with the wider community; ensure compliance with established policies, procedures, laws and regulations; identifying, evaluating and managing operational and financial risks and opportunities, including those arising from involvement in partnerships and joint ventures; ensuring compliance with the general duty of best value, where applicable; managing its financial and other resources, including arrangements to safeguard the financial standing of the local government body; monitoring and reviewing performance, including arrangements to ensure data quality; and ensuring that the audited body's affairs are managed in accordance with proper standards of financial conduct in order to detect and prevent fraud and corruption.

The IIA study (2006: 11) on the role of auditing in public sector governance, which was later supported by Khoury's study (2011: 44), suggested that, as an important element of a strong public sector, governance structure and auditing in government should strive to support the governance roles of oversight, insight and foresight. Because government's success is measured primarily by its ability to deliver services effectively and conduct programmes in an equitable and appropriate manner, government audit activities should have the authority and competency to evaluate

financial and programme integrity, effectiveness, and efficiency. Moreover, auditors must also protect the core values of the government, as it serves all citizens.

In a study conducted by Van Peurseem (2004: 378) internal auditors were asked to air their views on whether the functions they performed relating to internal audit engagements were essential, and to what degree. The findings of the study suggested that the characteristics of a “true” profession existed, but did not dominate. The study found that significantly, and as subgroups, public practice and experienced auditors may enjoy greater influence over management, and accountancy-trained auditors may enjoy greater status owing to the “mystique” of their activities.

A study by Hillison, Pacini and Sinason (1999: 351) on the role and responsibility of internal auditors with regard to the detection and prevention of fraud revealed that internal auditors, rather than external auditors, are more likely to detect and report the occurrence of employee fraud. They further identified that internal auditors should be able to recognise fraud risks that might occur, and provide assistance to external auditors through the implementation of Statements on Auditing Standards (SAS) No. 82.

The study conducted by IIA on public sector auditing (2006: 16) states, among other functions, that internal auditors performing within the public sector may provide objective, expert advice in various areas in which they possess expertise. Based on their knowledge and expertise, they may provide technical advice on issues related to good governance, accountability, ethical practice, and anti-corruption programmes; effective risk assessment and management; internal controls; sound business processes; information technology (IT) systems development and operations; project management; programme evaluation; and other areas affecting the effectiveness, efficiency, and economy of operations.

In addition, according to this IIA study, government auditors may provide services such as control and risk assessment workshops and training in areas such as fraud awareness, performance measurement and control design. They may also provide advice on implementing audit recommendations”. A study by Jayalakshmy, Seetharaman and Khong (2005: 269) on the changing roles and responsibilities of auditors summarised this section, indicated that “Internal auditors should feel equally responsible for the work they perform and should be answerable and equally professional.

Table 2.1 was developed to summarise the IAFs roles, as discussed.

Table 2.1: Expected roles to be performed by IAF

Role to be played by IAF	Description	Reference
Oversight role	Involves assisting the decision-makers in evaluating whether organisations are doing what they are supposed to do.	Study by the IIA on public sector auditing (2006), and study by Khoury, (2011).
Detection role	Involves the identification of inappropriate, unproductive, unlawful, fraudulent or abusive acts that have already transpired, and to gather evidence to support decisions regarding criminal prosecutions, disciplinary actions, or other remedies.	Study by IIA on public sector auditing (2006), and Hillison, Pacini & Sinason (1999).
Deterrence role	Intends to identify and reduce the conditions that lead to corruption.	Study by the IIA on public sector auditing (2006).
Insight role	Involves IAFs providing vision to help organisational management by assessing which programmes and policies are working and which are not, sharing best practices and benchmarking information.	Study by the IIA on public sector auditing (2006), and study by Khoury, (2011).
Foresight role	Identification of trends and bringing to management's attention emerging challenges before such challenges become crises.	Study by the IIA on public sector auditing (2006), and study by Khoury, (2011).

Source: (own research based on the quoted references)

Table 2.1 and the previous discussions enumerated the various roles expected of the IAF, such as oversight, detection, foresight, and deterrence. These roles are important in the IAF, and if competently carried out, the function is considered to be value-adding. The question that arises is do the IAFs at municipalities in South Africa perform these roles effectively?

2.8 INTERNAL AUDIT CHARTER

An Internal audit charter can be defined as a management-approved document that states the purpose of an IAF, its authority, and responsibility (Van der Nest, 2016: 149). The internal audit charter forms the foundation of the independence, operations, and communication lines of internal auditing". According to Flesher (1996: 493), "the management of IAF starts at the commencement of the function in a department. The chief audit executive (CAE) is responsible for obtaining a written charter for the IAF. This charter must be agreed upon with management and approved by the municipality's audit committee. This document spells out the purpose, authority, and responsibility of the IAF. In addition to the internal audit charter, the CAE must prepare a strategic plan and an annual coverage plan for the IAF.

The IIA attribute standard 1000 summarises the internal audit charter under Purpose, Authority and Responsibility as follows:

- Senior management, the board and the audit committee should approve the internal audit charter;
- The internal audit charter should be a formal document and must be in writing: approved and signed by all relevant parties;
- The charter should establish the position of the IAF within the municipality;
- Should define the scope of IAF's activities (1000.A1);
- Give unrestricted access to records, personnel etc. relevant to the performance of a specific engagement (1000.C1); and
- There should be ground rules within the municipality for consulting services and these should be documented in the internal audit charter as well.

The content of the internal audit charter assists IAFs in municipalities, and audit committees, to evaluate the entire IAF of the municipality. The objective of such an evaluation is to ensure that the IAF operates effectively. The evaluation should consider among others, the audit approach used and the audit coverage, the quality of reports during the year, quality of the personnel, cooperation with external auditors, and management satisfaction. The IAFs compliance with the Institute of Internal Auditors' Standards for the Professional Practice (IIASPPPI) should also be reviewed periodically". To assess the performance of the IAFs in the public sector and in municipalities, the audit committee could ask the following questions:

Table 2.2: Questions to review IAFs performance in the public sector and in municipalities

- “Are there formal terms of reference that define the objectives, responsibilities, authority and reporting lines of the IAF?”
- Are any restrictions placed on the work of the IAF?
- Has the scope of the IAFs work been determined by a risk-based approach, based on the standards of the IIA?
- What is the relationship between doing internal control reviews, value for money reviews and special projects?
- How is the internal audit’s independence guaranteed if requested to undertake special projects?
- Does the IAF report to an appropriate level of management that ensures audit recommendations are given due attention?
- Do internal audit staff have sufficient technical knowledge and experience to ensure that duties are performed in terms of the standards set by the IIA?
- Are there sufficient information systems for audit expertise to handle the IT systems of the municipality?
- Has the IAF provided a needs assessment?
- Is there a long-term strategic internal audit plan which schedules coverage of all areas identified in the risk assessment?
- Is the work of the IAF properly planned, completed, supervised and reviewed in terms of the requirements of the standards of the IIA?
- Are there quality assurance procedures in place?
- Are internal audit reports issued on time?
- Are the IAF reports followed up timeously, based on a systematic approach to follow up recommendations, and is there reporting on those which little or no action has been taken by management?”

Source: Van der Nest, 2006

Table 2.2, adopted from Van der Nest’s study (2006), provides questions that can be used to evaluate the effectiveness of the IAFs in the public sector, including municipalities. However, the questions posed do not consider other important elements that add to the functioning of IAFs, such as independence, reporting and what characterises a functioning IAF.

The following section discusses the value added by IAFs in organisations.

2.9 DETERMINING THE VALUE ADDED BY THE IAF IN AN ORGANISATION

Many researchers have explored ways in which to measure value-added by IAFs such as Roth (2003: 34) who claims that value-adding IAFs tend to share similar qualities. The concept of value-adding internal audits held by IAFs has direct relevance to internal audit effectiveness, because the latter serves as a measure of the former. Savcuk (2007: 277) agreed with this notion and believed that an IAF, being an integral part of corporate governance, can add value to an organisation only if it is effective.

A study by Popescu and Vasile (2011) on the internal audit value-added concept revealed that the value provided by the IAFs is represented by its capacity to improve the internal control systems of the organisations they serve. This study suggests that the IAF itself is the promoter of value-adding within an organisation by performing the following, among others: by creating opportunities for senior management to improve how things are done; by ensuring and advising management on how losses can be circumvented due to its actions; by ensuring transparency in the organisation's activities; and by contributing to make organisation's policies more efficient.

To reach the above-mentioned objectives which should be observed by every IAF, analyses and risk management, which represent a major concern for general management, need to be addressed.

The study (Popescu & Vasile, 2011) revealed that managers agree on the importance of creating and promoting an awareness culture within organisations. However, the people in charge of IAFs consider that managers do not pay enough attention to assessing the own risks, and that they do not consider the training of specialists a priority. The leadership activity is still empiric, and does not take into account the recommendations of the IAF and the terms of good practice recognised in this field. Internal auditors feel a need for modification in the organisational culture regarding risk assessment, but are not optimistic that managers' attitudes will improve in real time.

The value which the IAF adds to organisations has concrete ways and criteria for measuring this. The CAEs assess the value provided to organisations they serve, according to a series of indicators, as follows (Popescu & Vasile, 2011):

- General respect for the IAFs established within an organisation;
- The quality of audit findings and recommendations forwarded to management;
- Making up high quality reports, and delivering them in due time;

- Presenting reports to the broader management through the auditing committee;
- Attending the auditing committee meetings or those of the management board;
- Adding real value immediately;
- Pursuing opportunities to satisfy customers and beneficiaries;
- Higher savings and efficiency produced by the findings of the IAF, which are considered advance payment for the production costs;
- The number of letters received from other sections of organisation on respect of the IAFs contributions to business projects, etc.

The above-mentioned indicators raise several important questions, which need to be addressed for the IAF to be considered to be effective:

- “Is the IAF doing the right job?”
- Is the IAF providing value?
- How can the internal auditing prove its value to the business?
- How can the internal auditing convince us that they improved their activities”?

Through assessment of the future financial impact on the organisation, the value of IAFs can be measured in a way that proves the financial impact that would be produced for the organisation if the internal audit and internal controls or processes were modified or improved over a certain period of time. It must be noted that the implementation costs of new control activities can prove to be lower than those incurred before applying the respective changes. For example, if the IAF were to suggest changes to the way in which procurement processes are undertaken in order to improve controls, the function would then look at potential differences in costs savings over a projected period of one year. They would then report to management that purchase costs could be lowered by the amount derived from the calculations which, for instance, could be as much as 25%.

This view on value-adding is further supported by Ray (2009), who indicates that “there are various ways in which value-added by IAFs can be measured in reality. The main method is considered to be measurement of cost savings associated with the acceptance and implementation of the recommendations made by the IAF. Administering regular surveys to the departments being audited A way to establish the amount of value-added is to make regular surveys of the departments being audited. IAFs can also look into the extent to which external auditors rely on the work performed by the internal auditors”. The more reliance of the external auditors on the IAF work, the more the organisation saves in terms of cost and value-added by the IAF.

A study conducted by the IIA's Common Body of Knowledge (CBOK) in 2006, revealed the following, as shown in Table 2.3, regarding different ways in which the value-adding concept is measured in various organisations across the world:

Table 2.3: Measurement of value-added by IAFs worldwide:

Method of measuring value	Percentage
No formal measurement of value	33 %
Reliance by external auditors on the work of IAF	34%
Management requests for assurance/ consulting projects	27%
Assessments by customer surveys from audited departments	35%
Acceptance and implementation of recommendations	51%

Source: Ray, 2009 (CBOK)

Table 2.3) clearly indicates that the majority measured the value of IAF based on the acceptance and implementation of audit recommendations within their organisations.

As discussed above, many researchers have explored ways in which to measure value-added by IAFs, but Roth (2003: 34) claimed that value-adding IAFs tend to share similar qualities. Roth (2003: 34) further argued that the concept of value-adding in internal audits held by IAFs has direct relevance to the internal audit effectiveness, because the latter serves as a measure of the former. Savcuk (2007: 277) agreed with this notion and believed that an IAF, being an integral part of corporate governance, can add value to an organisation when is effective.

In a survey conducted in 2003 for the IIA Research Foundation (Adding value: Seven Roads to Success), information was solicited regarding best practices in value-adding internal auditing (Roth, 2003: 34). Roth (2003: 35–37) identified the following five value-adding characteristics for IAFs: organisational alignment; extensive staff expertise; challenging work environment; risk assessment of the audit universe; and an array of audit services. Dittenhofer (2001: 467–468) suggested that the following four attributes would make the internal audit process more useful and more efficient, and would improve its position vis-à-vis management's opinion of its value: adequate IAF interaction with the organisation; internal restructuring, creation of new services and methods; and using technology.

Gupta (2001: 62–73) suggested the following IAF value-adding characteristics: “assessing the inherent level of complexity in an organisation; identifying internal audit customers and their needs; developing a mission and vision for the IAF; taking a process view of the IAF; developing an internal audit business framework; using information technology as an enabler; and developing an appropriate internal audit strategic plan. In their study, Mihret and Woldeyohannis (2008: 573) applied the framework of attributes of a value-adding IAF developed by Roth (2003) to an Ethiopian case study. Mihret and Woldeyohannis (2008: 586–587) found that a traditional/compliance audit approach was dominant in the organization studied, and concluded that the goals and strategies pursued”, and the level of risk faced by an organisation appears to shape the value-adding attributes of an IAF.

In conclusion, the performance measurement methods used to measure the value-added by the IAFs are associated with their perceived contributions. While the more outcome-oriented methods show a higher correlation with the value statements, the remaining methods also have a median association with these statements. The results imply that although it is important for IAFs to use their resources efficiently, the outcomes of their work are imperative for the internal audit activities to provide value to the organisations they serve.

2.10 THE IAFS AND THE AUDIT COMMITTEES

The following section discusses the relationship between the IAFs and the audit committees, with reference to King IV Report (2016). It then proceeds with a discussion on the requirements of IAFs, according to the MFMA.

2.10.1 Relationship between IAFs and Audit Committees according to the King IV Report

The board of directors (the board) should ensure that it has an effective and independent audit committee, with approved terms of reference. The audit committee is perceived to be an integral part of the risk management process, with oversight of financial reporting risks, internal financial controls, and fraud and IT risks relevant to financial reporting (IOD, 2009). The IOD continues to require that IAFs should oversee: appointments and dismissals, performance management of the Chief Audit Executive (CAE); approve the internal audit plan; evaluate the document review of internal financial controls; assess internal audit performance and quality review the function to ensure it is properly resourced with sufficient budget; and monitor and review the effectiveness of the company’s IAF.

This implies that the audit committee is expected to play a crucial role in ensuring that the organisation's IAF is independent and has the necessary resources, standing, and authority within the organisation to enable it to discharge its functions. The audit committee is expected to oversee cooperation between external and internal auditing, to avoid the overlapping of audit functions. The audit committee should, therefore, formally consider the effectiveness of internal audits at least annually, and report to the board its assessment on the adequacy of the internal controls (IOD, 2009).

The King IV Report (2016) recommends that boards should ensure effective risk-based IAFs, governed by an internal audit charter approved by the board, which adheres to the IIA Standards and code of ethics. The IAF is expected to: report to the audit committee (CAE should report functionally to the audit committee chairman) and report at all audit committee meetings; evaluate the organisation's governance processes; objectively assess the effectiveness of risk management and the internal control framework; analyse business processes and controls and provide information on fraud and unethical practices. In addition, IAFs should have an internal audit plan that is informed by the strategy and risks of the organisation; be independent from management and objective at all times; provide the board with a written assessment on the effectiveness of the organisation's system of internal controls and risk management; and provide an annual written assessment of the internal financial controls to the audit committee after formally documenting and testing these controls (IOD, 2009).

Krishnamoorthy and Maletta (2008: 1) support the arguments by both the IOD and the MFMA, by stating that the greater the governance strength of the audit committee the greater the assessed quality of IAF and the greater the overall level of coordination between internal and external audit. Audit committee accounting expertise positively affects the level of internal/external audit coordination. The relationship between the audit committee and the IAF is vital in enabling the audit committee to meet its responsibilities. As such, the connection between the CAE and the audit committee is an important one. IAF is functionally responsible to the audit committee and works for the committee through its Head. Reports from the IAF provide the audit committee with a key source of information on the organisation's performance. Increasing the value of IAFs in organisations requires that open lines of communication are established and maintained between IAFs and the audit committees (<http://www.anao.gov.au>).

Based on the discussion above, it is evident that the audit committees are effective and are seen to be performing as planned if they are well serviced by an effective IAF. The IAFs, on the other

hand, need the support of the audit committees to perform their functions effectively. Therefore, both the IAFs and the audit committees work closely within organisations, to ensure that management is provided with pertinent information and valuable advice to assist in the operation of the business. A close and effective working relationship between the audit committee and the internal auditor is beneficial not only to the company which they serve, but also to the community as a whole. All this is possible if there is a good relationship between the two parties and they can rely upon each other.

In summary, the IAF, through chief audit executive (CAE), should maintain a good relationship with the audit committee and should strive for the following activities:

- “The CAE should have the dual responsibilities of reporting functionally to the audit committee and administratively to the municipal manager;
- The CAE should have ready access to the audit committee;
- The CAE should have direct and regular communication with the audit committee;
- The CAE should attend audit committee meetings;
- The CAE should meet privately with the audit committee (without management present) on a regular basis to discuss issues of common interest;
- The audit committee should approve the appointment or removal of a CAE; and
- The audit committee should be advised by the CAE on his relationship with the external auditors, and on how the internal and external audits are progressing”.

If such a relationship can be created within South African municipalities, both the IAFs and the audit committees will function optimally and add the expected value. Therefore, every municipality should strive for this relationship.

2.11 THE REQUIREMENTS OF AUDIT COMMITTEES ACCORDING TO THE MFMA

An audit committee reports to the board or governing authority of an organisation. It supports the organisational authority in performing the specific tasks related to internal control, risk, and governance, and oversees the work of the IAF (Lesejane, 2003). The definition of an audit committee is supported by sections 65 and 166 of the Municipal Finance Management Act No. 56 of 2003 (MFMA), which states that the audit committee operates as a committee of the municipal council. Audit committees are expected to perform the responsibilities allocated to them by the

MFMA (sections 165, 166), and the corporate governance responsibilities delegated by the council under its charter.

A charter as discussed above, as a document which defines the mandate, rights, aims, and principles of an organisation such as an audit committee, and in this case, is approved by a municipal council. The charter becomes the guiding policy of the audit committee, and informs the contracts of the audit committee members. A charter should be used to guide the activities of an audit committee on an ongoing basis. A clear, well-written charter should set out the objectives, roles and responsibilities, composition, structure, and membership requirements; relationships with other stakeholders; authority for the committee to conduct enquiries and access the municipality and the municipal entity's records and personnel; outline procedures for meetings; address the confidentiality and independence of committee members; and provide for ethical conduct and reporting.

Following its approval, the IAF's charter should be published on the municipal website to promote awareness of all the stakeholders within the organisation. The charter should "be reviewed annually and updated to ensure relevance, good practice, and consistency with the MFMA, Municipal Systems Act (No 32 of 2000), and other related regulators and guides. The charter should be used as a basis for: preparing the audit committee's annual work plan; setting the agenda for meetings; requesting skills and expertise; making recommendations to the accounting officer and municipal council; and assessing the audit committee's performance by its members". The Auditor-General, municipal council; management; and the internal auditors should all be aware of the charter and its contents.

2.11.1 Composition of an audit committee

Section 166 of the MFMA (2004), provides the requirements for the composition of an audit committee in a municipality. The audit committee must comprise at least three persons who are not employed by the municipality or a municipal entity. In terms of best practice, the number and size of a municipal audit committee can be increased to address the requirements, peculiarities and needs of the municipality or its entity, which will be guided by the approved charter. These requirements apply to all South African municipalities, regardless of whether the audit committee is established through a shared service or is outsourced through another mechanism.

2.11.2 Appointment of Audit Committee members

Section 166(5) of the MFMA requires that the audit committee's members must be appointed by the municipality's council or by the council of the parent municipality in the case of a municipal entity (MFMA). One of the members who is not working for the municipality or municipal entity, must be appointed as the chairperson of the committee. According to the MFMA the municipal councillors are not allowed to be members of an audit committee. The appointed members should enter into a contract with the municipality or municipal entity, according to the approved and formal terms of reference.

2.11.3 Reporting by Audit Committees

The chairperson of an audit committee should report to the municipal council on a quarterly basis, or more frequently if required, on the operations of the IAF and the audit committee. The report should include:

- A summary of the work performed by the IAF and the audit committee in compliance with the annual work plan;
- Effectiveness of internal controls and additional measures that must be implemented to address identified risks;
- A summary of key issues dealt with, such as significant internal and external audit findings and recommendations, and updated status thereof;
- Progress with any investigations and their outcomes;
- Details of meetings and the number of meetings attended by each member; and
- Other matters requested of the internal audit and audit committee.

The audit committee's chairperson must submit a copy of his/her report at least yearly or at any other agreed intervals, to the Municipal Public Accounts Committee (MPAC), for consideration during the MPAC engagement with the oversight report. The audit committee's chairperson must always be available whenever the MPAC needs answers on the report of the audit committee. Therefore, the roles, responsibilities and outputs of the IAF and the audit committee guide the work of the MPAC and other oversight structures.

2.11.4 The roles and responsibilities of audit committees in municipalities

The MFMA requires audit committees to perform the following roles and responsibilities, especially with regard to IAFs: (MFMA Circular 65, 2012):

- Ensure that the charter, independence, and activities of the IAF are clearly understood and respond to the objectives of the municipality and the legal framework;
- Regularly review the functional and administrative reporting lines of the internal auditor to ensure that the organisational structure is consistent with the principles of independence and accountability;
- Review and approve the internal audit charter, including the internal audit strategic plan;
- Confirm that the annual audit plan makes provision for critical risk areas in the municipality and its entities;
- Advise the municipality on resources allocated to give effect to the work outputs of the IAF;
- Ensure that there is support for the IAFs and external auditors from senior management;
- Confirm with management that internal audit findings are submitted to the audit committee on a quarterly basis;
- Confirm actions taken by management in relation to the audit plan;
- Consider and review reports relating to difficulties encountered during the course of the audit engagement, including any scope limitation or access to information reported to the accounting officer that remain unresolved;
- Evaluate the performance of the IAF in terms of the agreed goals and objectives as captured in the audit plan;
- Ensure that the head of internal audit has reasonable access to the chairperson of the audit committee;
- Conduct a high-level review of internal audit on an annual basis, to ascertain whether the IAF complies with the International Standards for the Professional Practice of Internal Auditing; and
- Concur with any appointment or termination of services of the CAE.

In addition to the responsibilities indicated above, the IIA Standards state that external assessments of the IAF should be conducted once every five years, but the need for more regular external assessments should be discussed by the CAE with the organisation's senior management (IIA (2003), section 1312).

On the other hand, the MFMA requires the IAF to be accountable to the audit committee as follows:

- Maintain open and effective communication with the audit committee;
- Develop a flexible annual audit plan using a risk-based methodology, addressing any weaknesses in risks or controls identified;
- Submit the audit plan to the audit committee for review and approval;
- Report on the implementation and results of the annual audit plan including special tasks requested by management and the audit committee;
- Assist in drafting the agenda and documentation, and facilitate the distribution thereof to the audit committee in advance of meetings;
- Meet periodically with the chairperson of the audit committee to discuss whether the material and information furnished meets the requirements of the audit committee;
- Obtain advice from the audit committee on whether the frequency and time allocated to the committee is sufficient to attend effectively to all matters;
- Cooperate with the audit committee as they conduct annual reviews of the performance of the IAF; and
- Submit the internal audit charter to the audit committee for review and approval on an annual basis and as necessary.

According to Nel (2011), the creation of audit committees in the government sector positively influences the increase of good governance within government sector in general. The transparent reporting by the audit committees has contributed to world markets' positive views of South Africa. However, the accountability attached to the accuracy and reliability of reporting being done is increasing, and is applying additional pressure on the IAFs to perform their tasks to the highest standards. The recent establishment of audit committees within the government sector in South Africa carries several opportunities and challenges for internal auditors (Nel, 2011). The senior management refers to audit committees for expert opinion and guidance, particularly on areas such as finance and risk management, and audit committees, in turn, expect expert comment and support from the IAF. Audit committees, play an integral part in the direct reporting line, and therefore have the chance to either "make or break" an IAF. The quality of audit committee members is critical, both to organisations and to IAFs. In the private sector, committee members are required to be board members, and their expertise can be attracted more easily as the private sector does not have the financial constraints applicable to the public sector.

It is clear from the roles and responsibilities of audit committees discussed above, that the reports of audit committees and the position of IAFs is strengthening. Audit committees, in accordance with the MFMA, are expected to support the IAFs and their functioning in municipalities to ensure that these IAFs play their expected role and are effective.

2.12 THE NEED FOR IAF IN SOUTH AFRICAN MUNICIPALITIES

A functioning IAF, good systems of internal control, and effective operation of an audit committee, are all important components of sound corporate governance in municipalities in South Africa. The MFMA requires that these important financial governance components should exist within all municipalities and every municipal entity in South Africa (MFMA Circular 65, 2012).

Section 165 of the MFMA requires that each municipality and each municipal entity must have an IAF. The IAF of a municipality or municipal entity must execute the following functions, among others:

- “Prepare a risk -based audit plan and an internal audit program for each financial year;
- Advise the accounting officer and report to the audit committee on the implementation of the internal audit plan and matters relating to:
 - Internal audit;
 - Internal controls;
 - Accounting procedures and practices;
 - Risk and risk management;
 - Performance management;
 - Loss control;
 - Compliance with this Act, the annual Division of Revenue Act, and any other applicable legislation; and
- Perform any such other duties as may be assigned to it by the accounting officer”.

Section 166 of the MFMA requires that each municipality and municipal entity must have an audit committee. The audit committee is expected to advise the municipal council, the political office bearers, the accounting officer, and the management of the municipality or municipal entity on matters relating to:

- “Internal financial control and internal audits;

- Risk management;
- Accounting policies;
- The adequacy, reliability and accuracy of financial reporting and information;
- Performance management;
- Effective governance; Compliance with the MFMA Act, the annual Division of Revenue Act and any other applicable legislation;
- Performance evaluation; and
- Any other issues referred to it by the municipality or municipal entity”.

It is evident that the IAFs in South Africa are audited in accordance with the requirements of the MFMA, which requires all municipalities to be audited both internally and externally to ensure that the municipalities’ goals are achieved, and accountability is maintained. Whether or not the audit committees perform every function indicated above, and the extent to which they rely on their IAFs, still needed verification. Thus, the study asked chairpersons of audit committees (as key stakeholders), if, from their perspective, the IAFs were providing their expected value.

2.12.1 The requirements for establishing IAFs in municipalities

Section 165 of the MFMA prescribes the requirements for establishing IAFs in South African municipalities. The IAF is seen as an important component of internal control, risk management, and corporate governance, and provides the essential assurances and advisory services to the municipalities.

The IAF is considered by MFMA as one of the most significant management mechanism that can provide value-adding services to the municipality or municipal entity. When objectively and sufficiently resourced, IAFs should be in a position to provide management with assurances regarding the effectiveness of the systems of internal control, risk management, and governance processes.

It is further expected that each internal auditor within the IAF should “have a neutral attitude and should be in a sufficiently independent position to be able to exercise judgment, express opinions, and present recommendations with impartiality. Every internal auditor should be free from any conflict of interest arising from professional or personal relationships or other interests which he/she may be subjected to audit and internal auditors should be free from undue influence which

could restrict or modify the scope or conduct of the audit work, or significantly affect judgment regarding the content of any audit report (MFMA)".

2.12.2 The independence and objectivity of IAFs in municipalities

The CAE of a municipality is required by the MFMA to report at a level within the municipality or municipal entity that will allow the IAF to fulfil its responsibilities. This level must have adequate authority to promote independence and to ensure wide coverage, satisfactory consideration of engagement communication, and suitable action on engagement recommendations. This requirement is further supported by the Attribute Standard 1110 of the ISPPA (2004) that states: "the CAE should report to a level within the organisation that allows the IAF to accomplish its responsibilities".

The CAE is required to "report functionally to the audit committee and administratively to the accounting officer. Independence is achieved through the organisational status and the objectivity of the IAF. An IAF is independent when it can carry out its work freely and objectively, and has the support of senior management and an audit committee. The CAE is expected to have direct communication with the accounting officer, audit committee, municipal council, and other appropriate governing authorities. This is further supported by Advisory Standard 1110-2 of the ISPPA, which recommends that besides having a functional reporting relationship with the audit committee, the CAE must have an administrative reporting relationship with senior management in order to achieve appropriate support to accomplish internal audit's day-to-day activities. Such support should include positioning the function and the CAE in the organisation's structure in such a manner that affords appropriate stature for the function within the organisation; for example, unrestricted access to staff, information, and documentation (Standards)".

Direct communication takes place when the CAE regularly attends and participates in meetings which relate to the oversight responsibilities for internal auditing, financial reporting, corporate governance, and control. The presence and contribution of CAE at these meetings provides an opportunity to exchange information concerning the plans and activities of IAFs (MFMA) to the senior management.

2.12.3 Organising the IAF in municipalities

According to the MFMA, the CAE needs to direct, oversee, and manage the activities of the IAF. These include amongst others, planning, resource management, application of operating policies

and procedures, appraisal of work, coordination of assurance activities and quality assurance. It is therefore expected that the CAE of the IAFs in municipalities should plan, manage the IAF resources, review the IAF work, and provide the assurance activities to enable the IAF to perform its functions fully, and add the expected value.

2.12.4 The development of internal audit strategic plans

The MFMA expects the CAE in municipalities to establish risk-based strategies to determine whether the priorities of the IAF are consistent with the municipality's goals. The IAFs' plan as well as the fieldwork, must focus on the risks to which the municipality is exposed. Developing a strategic audit plan follows a logical process, described below:

2.12.4.1 Understanding the Environment

The MFMA Circular 65 states that in order to identify the risks to which the municipalities are currently exposed to, and those to which they are likely to be exposed in the future, an understanding of the strategic plan and objectives of the municipalities must be obtained by the IAFs. A top-down view of the municipalities are taken, to better understand the operational risks and controls for managing those risks. This notion depicts the environment within which each municipality operates. A detailed risk analysis of the municipality is conducted to identify those risks that impact on the achievement of objectives. The data can be used to plan, direct a risk management approach, and provide the basis for risk management activities.

2.12.4.2 Developing operational internal audit plans

The MFMA Circular 65 recommends the development of operational internal audit plans by all the municipalities' IAFs. The operational internal audit plan is required to be based on an assessment of risks and exposures that may affect the municipality, and should be done at least annually in order to reflect the most current strategies of the municipality. Risk assessment is expected to be evaluated, with alignment of the operational plan to the overall objectives of the municipality ensured. The CAE must ensure that strategic and operational plans are developed annually, and are approved by the audit committees, and accepted by the accounting officers.

In developing operational internal audit plans the following key issues should be considered: the completeness of the risk assessment report of the municipality; the availability and skills of internal audit staff; the changes in the risk environment of the organisation, which means that the risk

environment should be evaluated on yearly basis; approval and acceptance of the operational plan by the audit committee; and the materiality of ad-hoc requests, as all of these could have a significant impact on the normal audit planning and timing process (MFMA Circular 65).

The MFMA Circular 65 states that the operational internal audit plan should be risk-based and must be developed taking into account the results of the risk assessments and the integrated plans so as to:

- Determine focus areas for internal audit activities;
- Determine internal audit scope in relation to the scheduled assignments;
- Allocate resources to planned audit assignments;
- Establish the timing of performance of the audit assignments; and
- Determine the reporting requirements and deadlines.

The MFMA Circular 65 advocates that operational internal audit plans should be tabled to management for comment prior to approval by the audit committee. The operational internal audit plan should be reviewed to identify any modification needed to reflect changing priorities and emerging audit needs. The audit committee should approve material changes to the operational internal audit plan.

Based on the discussion above, it is evident that the IAF plays an important role in municipalities in South Africa. These IAFs are expected to be independent and objective, and provide operational plans to assist municipalities in achieving their stated plans.

2.13 THE INDEPENDENCY OF IAFS

Standard 1100 of the IIA on independence and objectivity states: the IAF must be independent and internal auditors must be objective in performing their work". This standard emphasises the importance of the independence of IAFs in any organisation. Independence is interpreted to be the freedom from conditions that threaten the ability of the IAF to carry out internal audit responsibilities in an unbiased manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the IAF and the CAE, both should have direct and unrestricted access to senior management and the board within the organisation. This can be achieved through a dual-reporting relationship. Threats to independence must be managed at the individual auditor, engagement, functional, and organisational levels.

Objectivity refers to an unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others.

Standard 1110 continues to recommend that the CAE must report to a level within the organisation that allows the IAF to fulfil its responsibilities. The CAE must confirm this to the board, at least annually. This standard means that organisational independence within the organisation is effectively achieved when the CAE reports functionally to the board. Some of this functional reporting with regard to the board involves the following: approving the internal audit charter; approving the risk-based internal audit plan; approving the internal audit budget and resource plan; receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters; approving decisions regarding the appointment or removal of the chief audit executive; approving the remuneration of the CAE; and making appropriate inquiries of management and the CAE to determine whether there is inappropriate scope or resource limitations. This standard further recommends that the IAF must be permitted and enjoy unrestricted functioning in determining the scope of internal auditing, execution of its work, and communicating results.

The above-mentioned standards recommend and emphasise the important requirements that each IAF should comply with to be regarded as independent. However, a study by Christopher, Sarens and Leung (2009: 202) found that the independence of IAFs "is normally threatened by things such as using the IAF as a stepping stone to other positions; having the CEO or CFO approve the IAFs budget and providing input for the internal audit plan; and considering the internal auditor to be a partner, especially when these are combined with other indirect threats. With respect to the relationship with the audit committee, significant threats identified include CAEs not reporting functionally to the audit committee; the audit committee not having sole responsibility for appointing, dismissing and evaluating the CAE, and not having all audit committee members, or at least one member, qualified in accounting". This study therefore investigated the independence of IAFs in municipalities in South Africa, to determine whether these IAFs are functioning as per the discussed standards.

2.13.1 Public sector internal auditing

The International Organization of Supreme Audit Institutions (INTOSAI) (2012) recommends that the internal auditors in the public sector should be engaged to assist their organisations in improving their operations. The IAFs within the public sector are seen as an element of a strong

public sector governance basis. Most public sector's internal auditors are found to play a role in their organisation's accountability to the public as part of the check-and-balance process.

Similarly, the independence of IAFs within the government sector can be generally defined as freedom from dependence on, or influence or control by, another person, organisation, or state. Internal auditors work for, and primarily report to, the audited organisation. For internal auditors, independence is the freedom from conditions that threaten the ability of the IAF or the CAE to carry out internal audit responsibilities in an unbiased manner. Independence allows internal auditors to render the impartial and unbiased judgments essential to the proper conduct of engagements.

2.13.2 Importance of independence and objectivity in the public sector

The need for independence and objectivity in audit is important, irrespective of the level of government involved (ISSAI, 200/1). Independence and objectivity are important in ensuring that stakeholders perceive the internal audit work performed, and its results, as reliable, accurate, and impartial.

The nature of internal auditing and the role of providing impartial and accurate information on the use of government resources and services delivered, requires the IAF to perform their duties without any restrictions, free from interference or pressures from the organisation being reviewed, or from the area under audit (INTOSAI, 2012).

Therefore, the IAFs' knowledge and understanding of the organisation help in nurturing an effective relationships and in assessing and improving the effectiveness of risk management, internal controls, and governance processes. An organisation's employees are expected to bring challenges, information, and important matters to the attention of the IAF. In addition, an effective and well-run audit function will be sought out for services, information and guidance.

By providing impartial, neutral assessments of whether government sector operations and resources are responsibly and effectively managed to achieve planned results, the IAF can assist the government sector organisations such as municipalities to accomplish accountability and integrity, to improve operations, and instil confidence among residents and stakeholders.

2.13.3 Criteria for independence and objectivity

The International Standards of Supreme Audit Institutions (ISSAI, 1610) provides criteria to assess the objectivity of IAFs in the public sector. The criteria determine whether the IAF is established by legislation or regulation; is accountable to top management, for example the audit committee and

to those charged with governance; reports the audit results both to top management, for example the head or deputy head of the government organisation and those charged with governance; is located organisationally outside the staff and management function of the unit under audit; is sufficiently removed from political pressure to conduct audits and report findings, opinions, and conclusions objectively without fear of political reprisal; does not permit internal audit staff to audit operations for which they have previously been responsible, to avoid any perceived conflict of interest; and has access to those charged with governance.

INTOSAI (2012) suggests that in addition, the criteria to assess the independence of IAFs in the public sector may further include: clear and formally defined responsibilities and authorities of internal auditing in an audit charter; functional and personal segregation of internal auditing from responsibilities for management tasks and decisions (e.g. as heads of operational working groups in administrative reform projects); adequate freedom for the CAE in establishing audit plans; adequate payment and grading within the salary scale according to the responsibility and significance of internal auditing; and involvement and participation of the CAE in recruitment of audit staff.

2.13.4 How to achieve independence in the public sector

INTOSAI (2012) as the body representing all auditor-generals internationally, made the following suggestions with regard to achieving independence in the public sector:

2.13.4.1 Appropriate Placement and Organisational Status

The IAFs ability to achieve independence and objectivity depends on the appropriate placement and organisational status of the IAF within an organisation or in this case, in municipalities. The organisational status of the IAF should be sufficient to allow it to achieve its activities as defined by its audit charter. The IAF must be positioned in such a way that it may obtain cooperation from management and staff of the programme or entity being audited, and have free, unrestricted access to all functions, records, property, and personnel, including those charged with governance. Where practicable, those charged with governance such as audit committees, should exercise discretion and at least be consulted regarding the appointment, removal, and compensation considerations of the CAE. Consideration may also be given to employing a suitably organised, independent body to appoint the CAE. The CAE should be equal in rank to the senior management of the organisation. To avoid possible conflicts of interest, the CAE should report to a level in the organisation that allows the IAF to effectively carry out its responsibilities. The CAE should have

direct communication with those charged with governance. This communication strengthens the organisational status of internal auditing, enables full support and unrestricted access to functions, records, property, and personnel, and helps in ensuring that there is no damage to independence. It provides adequate authority to ensure wide audit coverage, adequate consideration of engagement communications, and appropriate action on recommendations.

2.13.4.2 Reporting Relationship

The IIA Standards state that the CAE must report to a level within the organisation that allows the IAF to fulfil its responsibilities. The CAE should report to executive management for assistance in establishing direction, support, and administrative interface; and to those charged with governance for strategic direction, reinforcement, and accountability. Those charged with governance such as the audit committee should safeguard the independence by approving the internal audit charter and (where applicable) the mandate. The IIA Standards requirements and other guidance, strongly recommend that to help maintain the independence of the IAF, its personnel should report to the CAE, who reports administratively to the CAE or equivalent, and functionally to those charged with governance.

2.13.4.3 Competency

The Code of Ethics of the IIA requires, and leading practices orders, that IAF practitioners should engage in those services for which they have the required expertise and experience; execute their duties in accordance with the Standards; and continually improve their expertise and effectiveness. The Standards require that IAF practitioners and the IAF, “collectively possess or develop the knowledge, skills, and other competencies needed to perform their responsibilities”. Competent and professional internal auditing staff, particularly those who adhere to the Standards, can help to ensure the success of the IAF.

2.13.4.4 Legislative Requirements

The legislative requirements to create a functioning IAF can assist securing the funding and independence of the IAF and recognise IAF as an important function in the government sector. Finally, adequate legal protection of internal audit practitioners’ independence, particularly under municipal service law such as the MFMA, is an important element of legislative frameworks that needs to be followed and applied.

2.14 CONCLUSION

This chapter focused on the origins of internal auditing, which were traced back to 4000 BC. Internal auditing was established in 1941, and thus is currently an established profession of approximately 75 years. The issuing of the IIA's statement of responsibility for internal auditors took place in 1947. The literature showed that development of the internal auditing profession's modern roots were formed in the 19th century, during the time of the Industrial Revolution, when the profession's growth was influenced by the increase in size and the decentralisation of organisations. The development of IAFs in the public sector in South Africa indicated that internal auditing in South Africa started in the 1990s, and was influenced by three main factors: the regulation of public entities (1993), the issuing of the King I Report (1994), and the establishment of AGSA (1996).

The chapter further discussed the value adding role of internal auditing, defining value as providing opportunities in order to achieve organisational goals, and ensuring that the IAF becomes the eyes and ears of senior management. The expected roles of IAFs, such as oversight insight, foresight, detection and deterrence were discussed. The determinants of the effectiveness of IAFs, such as organisational independence, senior management support, quality of audit work and professional proficiency of internal auditors were discussed. The methods of measuring the effectiveness of IASF were also discussed, including comparison of completed audits with the audit plan, the length of elapsed time before issuing audit reports, results from the auditees' surveys; the significance of audit findings; and recommendations made by IAFs. Further, key value-adding determinants in an organisation were identified. Finally, the chapter detailed the responsibilities and roles of audit committees, and the ways in which IAFs can assist the functioning of these committees.

Therefore, this chapter focused on the numerous themes that make up the IAF, and the effective roles that IAFs play within an organisation. Based on the literature, an empirical work was therefore conducted in this study to determine whether the IAFs in South African municipalities comply with the research and opinions expressed in the literature.

The following chapter (Chapter 3) considers the effectiveness of IAFs, and what other researchers and studies have found regarding how the effectiveness of IAFs can be measured. The chapter further discusses and enumerates all the existing municipalities in South Africa as at 31 December 2017.

CHAPTER 3

THE RULES AND REGULATIONS GOVERNING IAFS IN SOUTH AFRICAN MUNICIPALITIES

3.1 INTRODUCTION

The IAF is not expected to relieve or replace the senior management of their primary responsibilities of establishing and ensuring a sufficiently controlled environment within their areas of responsibility. However, it is still the duty of the senior management within the organisation to plan, organise and direct the performance of adequate controls to provide reasonable assurance that municipality's goals and objectives are accomplished in the most effective, efficient, and economical manner (MFMA).

The main contribution of IAFs to organisations should be to provide assurances on senior management's treatment of risk through governance and control processes. The IAFs are therefore, expected to provide and investigate the methods to deal with risks, such as decisions to terminate, transfer or tolerate risks, is their responsibility, and senior management must be advised on these aspects of response to risks. The result of this approach enables IAFs to focus on performing value-added, cost effective audits, aligned with the municipality's expectations, deliverables, strategic objectives and the risk profile of the municipality (MFMA).

On the other hand, all municipalities in South Africa are expected to follow and comply with the laws and regulations discussed below, such as: the ISPPA, MFMA, Municipal Systems Act, Municipal Property Rates Act of 2004, the Municipal Structures Act, and Treasury regulations, among others.

Due to the nature of this study, which was conducted within municipalities in South Africa, it is important to explain how IAFs should be established, based on the individual requirements of the types of municipalities existing in South Africa. This chapter describes the relevant laws and regulations which shaped the role of internal auditing within local government in South Africa, the different types of municipalities found in South Africa, and the specific roles played by each type of municipality. The chapter concludes with a discussion on other role-players who take part in municipalities in South Africa, such as the National Treasury, SALGA, AGSA, COGTA and audit committees. The section is followed by a discussion on the roles played by other role players in the functioning of municipalities in South Africa, and the interest they have in the effective running of IAFs.

The following section starts by discussing the laws and regulations that shape IAFs in South Africa.

3.2 LAWS AND REGULATIONS SHAPING IAFS IN LOCAL GOVERNMENT IN SOUTH AFRICA

The following laws and regulations are among those that shaped IAFs in the local government sphere in South Africa.

3.2.1 International Standards for the Professional Practice of Internal Auditing

The International Standards for the Professional Practice of Internal Auditing (ISPPIA) (Standards), are compulsory requirements for the professional practice of internal auditing and for evaluating the effectiveness of its performance. These standards were first developed in 1978, are regularly updated, and are regarded as the standard principles to be applied to individual IAF and activities.

As defined above, ISPPIA defines internal auditing as “an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes”.

Therefore, the ISPPIA emphasises the concept of adding value as the basis for IAF’s existence and needs to be persuaded every time in all organisations.

According to the Treasury Internal Audit Framework (2009: 23), the IAF should serve as the main source of information to audit committees (ACs) on the performance of an organisation. To maximise the value of IAF, it is vital that open lines of communication are established and maintained between the IAF and the AC.

The responsibilities of audit committees in relation to IAFs are as follows, among others (Internal Audit Framework, 2009):

- Act as a medium of communication between management, internal and external auditing;
- Review the internal audit strategic and operational plans, ensure that these plans are based on the organisation’s risk assessment, and approve them;
- Advise the Accounting Officer (AO) on the adequacy of internal audit resources needed to carry out auditing responsibilities, including the completion of the approved internal audit plans;
- Oversee the coordination of audit programmes conducted by internal and external audits;
- Review all high-risk audit reports and provide advice to the AO on significant issues identified in audit reports and action taken on issues raised;

- Monitor management's implementation of IAF recommendations;
- Review the internal audit charter to ensure that appropriate organisational structure, authority, access, and reporting arrangements are in place;
- Periodically review the performance of the IAF; and
- Provide advice to the AO on the appointment and/or dismissal of CAE.

3.2.2 Performance Standards

The following performance standards guide the IAF on how the internal audit work should be conducted:

3.2.2.1 Managing the IAF (Standard 2000)

This Standard states that the CAE must effectively manage the IAF to ensure it adds value to the organisation. This can be interpreted as the IAF being effectively managed by the CAE when the results of the IAF's work achieve the purpose and responsibility included in the internal audit charter. By following the definition of internal auditing and the Standards, the internal auditors in the IAF should demonstrate adherence to the Code of Ethics and the Standards. This interpretation further indicates that the IAF adds value to the organisation and its stakeholders when it provides objective and relevant assurance, and adds to the effectiveness and efficiency of governance, risk management and control processes.

3.2.2.2 Planning (Standard 2010)

This standard requires the CAE to establish a risk-based plan to determine the priorities of the IAF, which are consistent with the organisation's goals. This means that the CAE is responsible for developing a risk-based plan and should take into account the organisation's risk management framework, including using risk appetite levels set by management for the different activities of the organisation. If a framework does not exist, the CAE should use his/her own judgment of risks after consideration of inputs from those in authority. The CAE must then review and adjust the plan as necessary, in response to changes in the organisation's business, risks, operations, programmes, systems, and controls. The IAFs plan of engagement must be based on a documented risk assessment, undertaken at least annually. The comments of those in management must be considered in this process. The CAE must identify and consider the expectations of those in authority, and those of other stakeholders, for internal audit opinions and other conclusions. The

CAE should consider accepting proposed consulting engagements based on the engagement's potential to improve risk management, add value, and improve the organisation's operations

3.2.2.3 Overall Opinions (Standard 2450)

This IIA standard indicates that when an overall audit opinion is issued by the IAF, "it must consider the expectations of those in authority and other stakeholders, and must be supported by sufficient, reliable, relevant, and useful information". These items are regarded as the most important characteristics of any information contributed by the IAF, and should always be produced. This means that communication with all stakeholders should identify the scope, including the time period to which the opinion relates, the scope limitations, and consideration of all related projects including reliance on other assurance providers. Therefore, all IAFs should comply with the standards indicated above. The question that arises is whether IAFs within municipalities in South Africa adhere to these standards as expected.

3.2.2.4 Reporting to Senior Management and the Board (Standard 2060)

This IIA standard requires that the CAE report from time to time to organisational management and the board of directors on the IAF's purpose, authority, responsibilities and performance relative to its plan, with such reporting including significant risk exposures and control issues, including fraud risks, governance issues and other matters needed or requested by the organisation's management and the board of directors. This means that the content and the rate at which reporting is to be done, should be determined in discussion with the IAF, organisation's management, and the board of directors, depending on the importance of the information to be communicated and the urgency of the related actions to be taken by senior management or the board.

3.2.2.5 Understanding the stakeholders' expectations (Standard 2010)

Risk management and stakeholder expectations are the two primary drivers affecting the focus and direction of any IAF. As the specifics of drivers differ between individual departmental units, a fundamental underlying approach that recognises that unique internal audit solutions are required in each departmental unit situation is important. The "one size fits all" approach is not appropriate. The approach should be to obtain an understanding of management and other stakeholder expectations, including those from applicable departments.

This is achieved by discussion with the executive management and operational and functional management, to the extent considered necessary. The objective is to fully understand the significant drivers of the IAF. Initial efforts involve gaining an understanding of senior management and audit committee expectations of internal audit. Eventually, these significantly impact on the strategic direction, planning and customer focused processes of the IAF. Other stakeholders whose views may be solicited, include line management, regulators, and external auditors. It is, therefore, important for any IAF to fully understand what senior management and other relevant stakeholders expect from the IAF, and satisfy such expectations as much as possible.

3.2.3 Municipal Finance Management Act (MFMA)

According Section 2 of the MFMA Act (2013), the objective of the Act is to ensure that there is complete and sustainable management of the financial and fiscal affairs of municipalities and municipal entities, by establishing norms, standards, and other requirements to achieve the following aims, among others:

- Ensure transparent, accountable, and appropriate clear lines of responsibility in the fiscal and financial affairs of the municipalities and other municipal entities;
- Management of the municipalities' proceeds, expenditures, assets, and liabilities, and management of their financial affairs;
- Ensure good budgetary and financial planning processes and the coordination of those processes with the processes of state organs in other spheres of government;
- Ensure responsible borrowing;
- Handle financial problems in municipalities;
- Control of supply chain management processes; and
- Other financial matters.

This Act then recommends the establishment of IAFs in all municipalities in South Africa to be able to foresee and monitor all the above-mentioned requirements (Section 165 of MFMA).

Section 38 (1) (a) (ii) and 76 (4) (e) of the PFMA, as well as Section 165 of the MFMA, recommend the establishment of active IAFs within the government sector. According to the Act, the IAFs are an important component of internal control, risk management and corporate governance, and provide the necessary assurance and advisory services to the organisation. The IAF is viewed as one of the most important management tools and value-adding services to any organisation. When objectively and sufficiently resourced, an IAF should be in a position to provide management with the assurance it requires regarding the effectiveness of their systems of internal control, risk management and governance processes. The IAF must be well planned, organised, staffed, trained, directed, and monitored. The internal audits must be conducted in accordance with the standards set by the IIA, and the various Practice Advisories issued by the IIA, which provide much of the guidance required by IAFs for conducting their work.

All municipalities in South Africa should consider that the MFMA serves as the most important source of legislation, and it is expected that all municipalities and municipal entities follow and comply with the prescriptions of this Act.

3.2.4 The requirements of the MFMA

Section 165 of the MFMA recommends that IAFs should be established in all municipalities in South Africa. Internal auditing is considered by the MFMA as an important component of internal control, risk management, and corporate governance, and should provide all the necessary assurance and advisory services to the organisation. The IAF is one of its most significant management tools and can provide value-adding services to the municipality or municipal entity if well-used and well informed.

Considering the discussion above regarding the effectiveness of IAF in South Africa municipalities, the MFMA is an established internal municipal Act in South Africa that requires every IAF to prepare a risk-based audit plan and prepare an internal audit programme for each financial year that advises the accounting officers and reports to the audit committee on its implementation. Further, the audit plan must include matters relating to the internal audit, internal controls, accounting procedures and practices, risk and risk management, performance management, loss control, and compliance with the MFMA.

To increase the audit coverage with limited internal audit resources, the CAE should follow the risk-based audit approach as recommended by the MFMA (s165), and the IIA Standards. The objectives of risk-based internal auditing are to provide independent assurance to the accounting officers, senior management, and the audit committees of the municipalities, that all material risks are identified, and that the municipality will ultimately achieve its strategic objectives. As part of a risk-based approach, the first step is to conduct a risk assessment based on an all-inclusive framework covering the full range of the municipality's activities, from strategic to compliance risk. This identifies opportunities to improve stakeholder value by assessing the interactions between the drivers of stakeholder value and risk management in the context of both overall department strategy and the fiscal management process (IPPF).

Therefore, application of the above-mentioned approach is based on an understanding of the municipality's objectives, and should focus on those specific risks that may hamper the achievement of the objectives. And the development of an audit plan that responds to these and to the municipality's circumstances. The development of an audit plan must respond to the municipality's environment, and should be designed according to the internal auditor's professional judgment. In order to avoid a pure mechanistic performance of the audit approach, the internal auditor should re-evaluate the plan from time to time.

The following discussion elaborates on each point that was found important for this study, as listed in the MFMA.

3.2.4.1 Internal audit

According to the definition of internal auditing explained earlier, the IAF should play an important role in assessing and improving the effectiveness of risk management processes. In recent times, IAFs have proved to play an important part as a value-adding service in organisational structures (Al-Twajiry et al. 2003; Arena & Azzone, 2009; Coram, et al. 2008; Goodwin, 2004; Yee et al. 2007). Al-Twajiry et al. (2003) explain that there are two benefits in having an effective IAF within organisations. Firstly, it improves operations and assists in the management of risk. Secondly, it helps the organisation in the prevention and detection of errors or fraud, and in safeguarding the assets of the organisation.

It is expected, therefore, that the internal audit work of the IAF should be conducted in accordance with the standards set by the Institute of Internal Auditors. These are the standards referred to in the previous sections on the MFMA. The audit process includes engagement planning, performing

the engagement, monitoring, and communicating the results. Therefore, this study attempted to establish the extent to which this is done by IAFs in municipalities, as it is one of the key points that the MFMA requires for effective IAF performance.

3.2.4.2 Internal controls

The Committee of Sponsoring Organisations of the Treadway Commission's (COSO) integrated framework, defines internal control as a process effected by an entity's senior management that includes the board of directors, management, and other personnel, to provide reasonable assurance regarding the achievement of objectives in three main categories, namely: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations (COSO framework, updated 2013). This is further supported by the Institute of Directors (IOD, 2009) which states that the IAF should provide to the boards a written assessment of the effectiveness of the system of internal controls and risk management (King IV).

On the other hand, the objective of the IAF, among others, is to examine and evaluate the suitability and effectiveness of internal controls in order to provide the management of an organisation with information, analyses, and recommendations to assist them in achieving its objectives (Goodwin 2004; Yee et al. 2007). This is further supported by the IIA Standards, which state that the IAF must evaluate the adequacy and effectiveness of control regarding the: reliability and integrity of financial and operational information; effectiveness and efficiency operations; safeguarding of assets; and compliance with laws, regulations, and contracts.

Based on adverse and disclaimer audit opinions by the AGSA (AGSA, 2011: 32; Auditor-General South Africa, 2012: 86; Auditor-General South Africa, 2013: 31, 35, 75, 103), this study intended to establish among others if municipal IAFs comply with the provisions of the MFMA and the IIA Standards.

Based on the results of a risk assessment, the IAF must appraise the appropriateness and effectiveness of controls surrounding the municipality's governance, operations, and information systems. In assessing the suitability of the control environment and management's approach towards controls, standard control practices and compliance with other generally used control frameworks should be taken into consideration.

If the controls are sufficient, the IAF should appraise the internal controls for effectiveness. To ensure that the conclusions reached are correct and supported by acceptable evidence, the

internal auditors are required to examine and appraise the findings of the audit in order to determine whether the internal controls are effective or not. The internal auditor may reach the following conclusion when evaluating the controls for effectiveness. If the existing controls are effective, the internal auditor will conclude that they provide reasonable assurance that the activity being audited will accomplish its performance objectives.

3.2.4.3 Accounting procedures and practices

One of the five guidelines from the IIA's Statement of Responsibilities of Internal Auditing, which should be included in all the internal audit charters, is to assess the trustworthiness and honesty of financial and operating information, and the means used to identify, measure, classify, and report such information. It is therefore, expected that IAFs will perform this command fully and completely.

The Accounting Standards Board (the board) is required, in terms of the Municipal Finance Management Act No. 56 of 2003, as amended (MFMA), to determine generally recognised accounting practices (GRAP). The municipal council must determine the GRAP for municipalities among others. It is therefore expected that the IAF should review the reliability and integrity of financial information as reported using GRAP, and report any deviation to those in authority at the municipalities. This function is seen as one of the most important procedures to be undertaken by every effective and working IAF operating within municipalities.

3.2.4.4 Risk and risk management

According to the MFMA circular 65 of 2003, the IAF is responsible for providing assurance to management and the audit committee on the sufficiency and effectiveness of the risk management process within the municipality. Risk management is a main responsibility of both the accounting officer and management. Management should ensure that adequate risk management procedures are in place and are functioning as planned (MFMA).

Conducting assessments and reporting on the organisation's risk management process should be a high priority of every IAF. Risks arising from business strategies and activities should be identified and prioritised, and the focus should be on efficient, economic and effective use of resources, and avoidance of any duplication of functions. Management should determine the level of risk acceptable to the municipality, risk mitigation activities should be designed and implemented

to reduce or manage risk at a level acceptable to the municipality, and management should receive periodic reports on the results of the risk management processes.

This is further supported by the Treasury's Internal Audit Framework (South Africa, 2009) which states that the IAF must help both management and the audit committee by examining, assessing, reporting, and recommending improvements on the sufficiency and effectiveness of management's risk processes. The IAF must be satisfied that the organisation's risk management procedures address five main objectives in order to formulate an opinion on the overall sufficiency thereof.

3.2.4.5 Performance management

Among other responsibilities, audit committees have the responsibility to review performance management. The municipality is expected to evaluate its committees and combine the audit committee and the performance audit committee for effective management, oversight and reporting, as outlined in section 166 of the MFMA.

Audit committee members need to have a good understanding of the performance of their municipality and its entities. Their functions include evaluation and comment on compliance with statutory requirements; performance management best practices and standards; and comment on the alignment of the integrated development plan with budget; service delivery; and the budget implementation plan. Performance agreements must be reviewed and comments made on the relevance of indicators to ensure they are measurable, and relate to services performed by the municipality and its entities. Quarterly performance reports submitted by the internal audit need review, and comment made on the municipalities and entities' annual financial statements and reports must be made within the stipulated time frame. This is concluded timely through submission to the Auditor-General by 31 August each year.

All the above-mentioned responsibilities can unquestionably be delegated to the IAF, which should ensure that all the responsibilities mentioned are completed on behalf of the audit committee to ensure that the IAF is adding the required value. This study among others intends to establish if these responsibilities are indeed being performed within the municipalities.

3.2.4.6 Loss control

The following directive from the IIA's Statement of Responsibilities of Internal Auditing, is expected to be included in all internal audit charters of all the municipalities: evaluate the means of

safeguarding assets and, as suitable, confirm the existence of such assets and assess the economy and efficiency with which resources are employed. This means that the IAF should evaluate the means used to protect assets from various losses such as fire, theft, unsuitable or unlawful activities and exposure to elements, and verify the existence of such assets by using the suitable audit procedures.

The MFMA circular 65 recommends that the observations and recommendations made by the IAF that need immediate action should be monitored by the IAF until fully concluded. To avoid losses, the IAF should ensure that actions taken by management timeously address the identified deficiencies. A process should be developed for the implementation of management action plans. Responsibility for follow-up should be defined in the internal audit charter. Follow-up audits involve confirmation of implementation of management actions, and must be combined in the annual internal operational audit plan. It is therefore expected that the IAF should assist organisations, in this case the municipalities, with measures to ensure that they do not experience any losses.

3.2.4.7 Compliance with acts and regulations including the MFMA

The Internal Audit Framework (2009) was formulated by South African Treasury with the aim of providing and establishing minimum guidelines for the development and operation of internal auditing in the public service. The framework serves as a source of reference and is a distinguished guiding instrument on internal auditing in the public service in South Africa. It is intended to ensure that IAFs comply with the requirements of the Constitution of the Republic of South Africa (1996); the Municipal Finance Management Act 56 of 2003 (MFMA); the Institute of Internal Auditors (IIA); the International Standards for the Professional Practice of Internal Auditing (ISPPIA); and the COSO Internal Control Framework.

The following directive is one of the five directives from the IIA's Statement of Responsibilities of Internal Auditing, which are included in most internal audit charters: evaluate the systems established to ensure compliance with those policies, plans, procedures, laws, regulations and contracts which could have a major impact on operations and reports, and determine whether the organisation is in compliance. This study intended to establish among others, if this directive is performed by the IAF at municipalities in South Africa, and to determine whether such IAFs are effective in performing their functions.

3.2.5 The Local Government: Municipal Systems Act No. 32 of 2000

The Municipal Systems Act was promulgated in 2000 to enable municipalities in South Africa to provide social and economic support where necessary for the benefit of residents within municipalities. The Act aims to achieve the following, among others:

- Provide for the basic principles, mechanisms and processes that are necessary to enable municipalities to provide social and economic improvement of local communities and common access to essential services that are affordable to all people residing in the municipality;
- Define the legal nature of a municipality as including the local community within the municipal area;
- Provide for the manner in which municipal powers and functions are exercised and performed;
- Provide for community participation;
- Provide a framework for local public administration and human resource development;
- Empower the poor and ensure that municipalities put in place service tariffs and credit control policies that take their needs into account by providing a framework for the provision of services and service delivery agreements;
- Establish a framework for support, monitoring and standard setting by other spheres of government; and
- Provide for legal matters pertaining to local government; and provide for matters incidental thereto.

As indicated, the Act was to ensure that the municipalities established within communities devised tangible ways of assisting those communities in uplifting lives in general, and providing service delivery. All the necessary processes and protocols needed by a municipality to fulfil its mandate are fully explained in this Act. All municipalities in South Africa are expected to comply with this Act.

3.2.6 Local Government: Municipal Structures Act No. 117 of 1998

This Act was promulgated in 1998 with the aim of providing guidance on the establishment of different types of municipalities as allowed by the Constitution of South Africa. The aim of this Act is to:

- Provide for the establishment of municipalities in accordance with the requirements relating to categories and types of municipality;
- Establish criteria for determining the category of municipality to be established in an area;
- Define the types of municipality that may be established within each category; provide for an appropriate division of functions and powers between categories of municipality;
- Regulate the internal systems, structures, and office-bearers of municipalities; and
- Provide for appropriate electoral systems and provide for matters in connection therewith (Municipal Structures Act, 1998).

As discussed in this chapter, the requirements necessary for the establishment of a municipality were fully discussed. The Act further explains the powers and functions each municipality has within its authority. As indicated above, the Act further outlines and regulates how the office bearers in different municipalities should conduct their work. It is therefore expected that all municipalities found in South Africa are established in accordance with the provisions of this Act.

3.2.7 Local Government: Municipal Property Rates Act, 2004

The Municipal Property Rates Act of 2004 is aimed at regulating the power of a municipality by imposing rates on properties; excluding certain properties from rates, in the national interest; making provision for municipalities to implement a transparent and fair system of exemptions; allowing reductions and rebates through their rating policies; making provision for fair and equitable property valuation methods; making provision for objections and appeals processes; amending the Local Government: Municipal Systems Act, 2000, so as to make further provision for the serving of documents by municipalities; amending or repealing certain legislation; and providing for matters connected therewith (Municipal Property Rates Act, 2004).

The Municipal Property Rate Act provides the basis for property evaluations within the municipalities with the aim of ensuring equity and fairness. This Act ensures that the rates charged by different municipalities consider different areas and are fair and transparent to everyone. All municipalities are expected to comply with this Act and to be transparent in their evaluation.

3.2.8 Treasury regulations

Section 168 (1) of the MFMA provides powers to the Minister of Finance, acting in consultation with the cabinet member responsible for local government (mainly the Minister of Local Government), to formulate regulations or guidelines applicable to municipalities and municipal entities, regarding the following:

- (a) Any matter that may be prescribed in terms of this Act;
- (b) Financial management and internal control;
- (c) A framework for regulating the exercise of municipal fiscal and tariff-fixing powers;
- (d) A framework regulating the financial commitments of municipalities and municipal entities in terms of public-private partnership agreements;
- (e) The establishment by municipalities of, and control over:
 - (i) Municipal entities; and
 - (ii) Business units contemplated in section 76(a) (ii) of the Municipal Systems Act;
- (f) The safe-guarding of the financial affairs of municipalities and of municipal entities when assets, liabilities or staff are transferred from or to a municipality or a municipal entity;
- (g) The alienation, letting, or disposal of assets by municipalities or municipal entities;
- (h) IAFs and their functioning;
- (i) The information to be disclosed when municipalities or municipal entities issue or incur debt and the manner in which such information must be disclosed, including by way of a prospectus or other document;
- (j) The circumstances under which further or specific disclosures are required after money has been borrowed by a municipality or municipal entity;
- (k) The circumstances under which documentation or information pertaining to municipal debt must be lodged or registered;
- (l) The establishment of a registry for the registration of documentation and information pertaining to municipal borrowing;
- (m) The settlement of claims against a municipality following an order of court in terms of section 153;
- (n) The information that must be placed on the websites of municipalities;
- (o) A framework regulating investments by municipal entities; and
- (p) Any other matter that may facilitate the enforcement and administration of this Act.

This indicates that the Department of National Treasury plays a key role in ensuring that municipalities and all other government entities in South Africa operate according to the laws and

regulations, and play a monitoring role to ensure that they comply with those laws and regulations. Where any gap exists in the application of a particular law or regulation, the Department is there to remedy it through additional guidelines or instructions that are occasionally sent to municipalities.

3.2.9 The Auditor-General South Africa (AGSA)

3.2.9.1 Mandate of AGSA

The Auditor-General South Africa (AGSA) is the South African's supreme audit institution, with its authority detailed in the Constitution of the Republic of South Africa (Constitution, 1996). In terms of section 181 of the Constitution, the AGSA is a state institution in South Africa established to reinforce constitutional democracy in the Republic. Section 188(1) of the Constitution (1996) states that the AGSA must conduct audit and report on the accounts, financial statements, and financial management of the following:

- all national and provincial state departments and administrations;
- all municipalities; and
- any other institution or accounting entity required by national or provincial legislation to be audited by the Auditor-General.

The AGSA office was set up in terms of Chapter 9 of the South African Constitution (1996). As a Chapter 9 institution, it was set up to safeguard the country's constitutional democracy. (<http://www.southafrica.info/about/democracy/auditorgeneral.htm#ixzz3zC09CfVn>)

The independence of the Auditor-General is guaranteed by the Constitution, which states that the Auditor-General must be impartial and must exercise its powers and perform its functions without fear, favour or prejudice.

The AGSA's constitutional requirements involves the passing of the Public Audit Act (Act 25 of 2004). This Act was propagated to give effect to the requirements of the Constitution (Constitution, 1996), establishing and assigning functions to the AGSA's office. Section 2 of the Public Audit Act (SA, 2004) list the objectives of the Public Audit Act as:

- (a) to give effect to the provisions of the Constitution (Constitution, 1996), establishing and assigning supreme auditing functions to an Auditor-General;
- (b) to provide for the auditing of institutions and accounting entities in the public sector; and
- (c) to provide for an oversight mechanism established in terms of section (3)

(d) to assist and protect the Auditor-General in order to ensure the independence, impartiality, dignity, and effectiveness of the Auditor-General; and to advise the National Assembly.

Section 3 of the Public Audit Act (25 of 2004) confirms the Constitutional and legal status of the Auditor-General as follows:

The Auditor-General

(a) is the supreme audit institution of the Republic;

(b) has full legal capacity, is independent and is subject only to the Constitution (Act 108 of 1996) and the law, including this Act;

(c) must be impartial and must exercise the powers and perform the functions of office without fear, favour, or prejudice; and

(d) is accountable to the National Assembly.

This pledges that the independence of the Auditor-General South Africa is enforced by statute. The functioning and powers of the Auditor-General are also regulated. Therefore, this legislation contributes to the accountability of the public service and strengthens democracy in South Africa. In addition to the above legislation, the Public Finance Management Act (Act 1 of 1999) (SA, 1999: Sec 58) indicates that the annual financial statements of a department must be audited each year by the Auditor-General or any person registered in terms of the Public Accountants' and Auditors' Act, (Act no 80 of 1991), but only if the audit is not performed by the Auditor-General.

The MFMA has a regulation for the economical, effective, and efficient use of resources in a municipality. The Auditor-General reports on "whether the municipality's resources were acquired economically and utilised efficiently and effectively (SA, 2004 sec. 20). This increases the Auditor-General's reporting powers in addition to reviewing the fair presentation of financial statements. It is clear from the above that the Auditor-General is independent of the public service and in terms of accountability", as he/she reports directly to the parliament and without possible interference by any political office-bearer.

3.2.9.2 The administration and reports by AGSA

According to the Public Audit Act (PAA, 2004), as from 2006, all the public-sector audits including those of municipalities should go beyond only expressing an opinion on the financial statements. While conducting its audits, the AGSA should also comment on the effectiveness of key

management processes and give feedback on compliance with laws and regulations, including comment on the IAF as one of the management tools available. The AGSA should, therefore, report in a manner that enables parliament and the executive to account for how they deal with taxpayers' money. The AGSA's annual and discretionary reports are tabled to the legislature with direct interest in the audit; that is, parliament and provincial legislatures or municipal councils depending on the level at which the audit has been conducted. These reports are then used by the legislature in accordance with their own rules and procedures for oversight.

Summary

The above discussion focused on the different laws and regulations that exist in South Africa, which shape the smooth functioning of the municipalities. The laws and regulations were identified as the ISPPA; the MFMA; the Municipal Systems Act of 2000; the Municipal Property Rates Act of 2004; the Municipal Structures Act of 1998; Treasury regulations, and the AGSA. These laws and regulations play an important role in ensuring that the municipalities function and render the required services and improve the lives of their own communities. It is evident that the IAFs should play an important role in ensuring that all these laws and regulations are followed and complied with in municipalities, and confirm that all objectives are realised.

It is important to discuss and explain the nature and types of municipalities that exist in South Africa today, since this study was conducted in many of the different types of municipalities.

3.3 MUNICIPALITIES IN SOUTH AFRICA

3.3.1 Spheres of government in South Africa

The Constitution of South Africa identifies the country's three spheres of government: The National government, Provincial government, and Local government. (Constitution, 1996).

These three spheres of government are autonomous and should not be seen as hierarchical. The Constitution indicates that these spheres of government are distinctive, interconnected and inter-dependent, and at the same time, they all operate according to the Constitution and laws and policies made by the South African parliament.

The government's functioning in South Africa is made up of three parts, namely:

- The elected members (legislatures) who represent the public, approve policies and laws, and monitor the work of the executive and the departments.

- The Cabinet or Executive committee (executive) who coordinate the making of policies and laws and oversee implementation by the government departments.
- The departments and public servants who are responsible for doing the work of government and account to the executive.

Table 3.1: Spheres of government in South Africa:

Sphere	Legislature	Executive	Administration
National government	Parliament	President and Cabinet	Directors General and national departments
Provincial government	Legislature	Premier and Executive Council	Heads of departments and staff
Local government	Council	Mayor and Mayoral Committee	Municipal Manager, Heads of Departments (HoDs) and staff

Source: The Constitution of South Africa (1996)

3.3.2 Local government in South Africa

The South African Constitution of 1996 provides direction on the position of local government in South Africa. Section 151 of the constitution states that “the local government sphere consists of municipalities, which must be established for the whole of the territory of the Republic, and the executive and legislative authority of a municipality, which is bestowed on its municipal council”. This section provides the municipalities with special privileges to administrate based on their own initiative and the affairs of their communities, subject to compliance with the national and provincial governments.

The Constitution further offers various types of municipalities that can be established in South Africa (The Constitution, 1996: s155 par. 1) as follows: category A is a metropolitan municipality, which can be described as a municipality that has exclusive municipal executive and legislative authority in its area; category B is a municipality that shares municipal, executive, and legislative authority in its area; category C is a municipality that has municipal, executive, and legislative authority in an area that includes more than one municipality.

A major difference between these types of municipalities which needs to be clarified, is the fact that category A municipalities are metropolitan municipalities, and have exclusive municipal, executive, and legislative authority in their area. This type of municipality was, to a large extent, developed to

carry out the White Paper on Local Government, on the cabinet's broad objectives, which include that: metropolitan governments should create a basis for equitable and socially just metropolitan governance; promote strategic land use planning and coordinated public investment in physical and social infrastructure; and develop a city-wide framework for economic and social development that enhances the economic competitiveness and well-being of a city (South Africa, 2008).

South Africa presently has eight category/type "A" metropolitan municipalities (South Africa, 2013). According to the Municipal Structures Act 117 of 1998, the following criteria must be met for a municipality to be declared a category A municipality (South Africa, 2008; 1998: s2). It should be a municipality containing places of high population density with an intense movement of people, goods, and services; it should have continuing extensive growth, with numerous business regions and industrial areas; it should be the heart of economic action, with a complex and varied economy; it should be a single area for which integrated development planning is required; and should have strong interdependent social and economic relations between its integral units.

The above-mentioned criteria summarise the reasons why the researcher wants to study among others the effectiveness of IAFs in these types of municipality.

If a municipal area is not classified as a category A municipality, the area is classified as having a category B or C municipality. Being a category A municipality makes the area a city which is a very large urban area compared to smaller, more rural categories B and C (South Africa, 2013).

As highlighted by the AGSA report, it is evident that there are some shortcomings within the municipalities in South Africa, and a conceptual framework was developed to address these shortcomings.

3.3.3 Powers of the municipalities in South Africa

According to the Local Government Municipal Structures Act of 1998, South Africa is divided into local municipalities. Each municipality has a council made up of elected members who approve policies and by-laws for their specific area, and municipal officials and staff who implement the work of the municipality the council has the power and responsibility to pass a budget for its municipality each year and decide on development plans and service delivery for their municipal area, among other functions.

The work of the council is coordinated by a mayor, who is elected by the council. The mayor is assisted by councillors in an executive committee appointed by the council or the mayoral

committee. The mayor together with the executive or mayoral committee oversee the work of the municipal manager and department heads. In some small municipalities, the council itself works under a plenary system, in which executive powers are vested in the full council. The work of the municipality is done by the municipal administrative body under the supervision of the municipal manager and other officials. The manager is responsible for employing staff and coordinating them to implement all programmes approved by the council (Local Government Municipal Structures Act of 1998).

3.3.4 The role of municipalities in South Africa

There were 285 municipalities in South Africa, including all categories of municipalities, as at December 2017, (Annexure B), i.e. category A, B, and C municipalities. They are established by government with the aim of growing local economies and providing infrastructure and services. The Constitution provided for three categories of municipalities in the Local Government Municipal Structures Act of 1998, which contains the criteria for determining when an area is a category A municipality (metropolitan municipalities) and when municipalities fall into categories B (local municipalities) or C (district municipalities). Table 3.2 below shows the roles and the responsibilities within South African municipalities.

Table 3.2: Roles within a municipality

List	Public sector	Role/Responsibilities
1	Council	Ensure overall running of municipality
2	Mayor	Strategic Oversight
3	Municipal Manager	Strategic Leadership
4	Heads of departments	Execute Strategy
5	Senior managers	Implement Strategy
6	Employees	Performance of Duties
7	Community	Recipient of Services

Source: Ameer Mahabir (2010)

3.3.5 Functions of municipalities in South Africa

According to the Local Government Municipal Structures Act of 1998, municipalities in South Africa are responsible for the following functions:

- Provision of electricity;
- Provision of sewage and sanitation services;
- Provide refuse removal;
- Provide municipal health services;
- Provide municipal roads;
- Regulate street trading;
- Provide parks and recreational facilities;
- Supply water for household use;
- Provide storm water systems;
- Provide fire-fighting services;
- Make decisions around land use;
- Provide municipal public transport;
- Regulate abattoirs and fresh food markets; and
- Provide libraries and other facilities.

3.3.6 Different types of municipalities in South Africa:

According to the Local Government Municipal Structures Act (1998), there are three different types of municipalities in South Africa, namely:

3.3.6.1. Metropolitan municipalities (Category A):

Metropolitan municipalities exist in the eight biggest cities in South Africa. They are municipalities that each have more than 500 000 voters. These metropolitan municipalities coordinate the delivery of services to the whole municipal area. There are metropolitan municipalities in Johannesburg, Cape Town, Ethekwini (Durban), Tshwane (Pretoria), Nelson Mandela (Port Elizabeth), Buffalo City, Ekurhuleni (East Rand), and Mangaung (Bloemfontein).

According to the Parliamentary Liaison Office's briefing paper of September 2000 on the challenges facing new municipalities at that time, a metropolitan council had exclusive and sole authority in its area of jurisdiction. This meant that all metropolitan areas were governed by one strong structure, which had overall responsibility for all the communities within that area.

Metropolitan councils created sub-councils to carry out the functions that the metropolitan council delegated to them. Following a public consultation process, each metropolitan decided on the number of sub-councils to be established, as well as the area which each sub-council was to cover.

This system differs “from the current two-tiered system in which metropolitan “local councils” or “sub-structures” are fully-fledged, directly elected municipalities, and the ‘greater metropolitan councils’ are more like umbrella structures incorporating a number of local councils. In future, the sub-councils will be chiefly administrative structures for the delivery of services, although they may also play a consultative role. Metropolitan councils will play a much bigger role and have greater political powers. This new metropolitan framework has become known as the ‘uni-city’ framework. These municipalities are broken into wards. Half the councillors are elected through a proportional representation ballot, where voters vote for a party. The other half are elected as ward councillors by the voters in each ward”.

3.3.6.2. Local municipalities (Category B):

Areas that fall outside of the eight metropolitan municipal areas indicated above are divided into local municipalities. There were a total of 230 of these local municipalities as at December 2016, with each municipality divided into wards. The residents in each ward are represented by a ward councillor. Only people who live in low population areas such as game parks, do not fall under local municipalities. The areas are called district management areas (DMA) and fall directly under the district municipality.

Local municipalities (Category B) are established in and around towns that have their own viable economy and infrastructure. The Demarcation Board has determined boundaries for all the local municipalities in South Africa. In most cases, the boundaries for local municipalities have been expanded, to ensure more efficient and integrated provision of services within towns and their immediate surrounding areas (Briefing paper 35).

In local municipalities, half the councillors are chosen through a proportional representation election, where voters vote for a party. The other half are elected as ward councillors by the residents in each ward.

3.3.6.3. District municipalities (Category C):

District municipalities are made up of several local municipalities that fall in one particular district. There are usually between three to six local municipalities that come together in a district council.

There were 47 district municipalities in South Africa as at 31 December 2015. Some district municipalities also include nature reserves and areas where few people live. These fall directly under the district council and have no local council. The district municipality coordinates development and delivery in the whole district. It plays a stronger role in areas where local municipalities lack capacity to deliver. It has its own administration staff.

District municipalities play an important role in assisting and supporting local municipalities in fulfilling their obligations. According to the Municipal Structures Act, district municipalities must seek to achieve integrated, sustainable, and equitable development for their entire area by:

- “Ensuring integrated development planning for the whole district;
- Promoting bulk infrastructural development and services;
- Building capacity of local municipalities its area; and
- Promoting equitable distribution of resources between local municipalities and DMAs. (Briefing paper 35)”.

The district Council is made up of two types of councillors:

- “Elected councillors who are elected to the district council on a proportional representation ballot by all voters in the area (40% of the district councillors)
- Councillors who represent local municipalities in the area – they are local councillors sent by their council to represent it on the district council (60% of the district councillors)”.

While metropolitan municipalities are responsible for all local services development and delivery in metropolitan areas, local municipalities share these responsibilities with district municipalities. This is especially the case in very rural areas, where district municipalities have more responsibility for development and service delivery.

3.3.7 Municipalities in South Africa per province:

South Africa had the following municipalities as at 31 December 2017. A complete list of these municipalities is listed in Appendix A. Table 3.3 shows these municipalities by location and type.

Table 3.3: All municipalities in South Africa:

Province	Type A	Type C	Type B	Total
Eastern Cape	2	7	38	47
Free State	1	5	20	26
Gauteng	3	2	7	12
Kwazulu-Natal	1	11	51	63
Limpopo	-	5	25	30
Mpumalanga	-	3	18	21
North-West	-	4	19	23
Northern Cape	-	5	27	32
Western Cape	1	5	25	31
Total	8	47	230	285

Source: own calculation

Table 3.3 indicates that there is a total of eight metropolitan municipalities, 47 district municipalities and 230 local municipalities in South Africa as at 31 December 2017.

3.3.7.1 Summary

The above discussion focused on existing South African municipalities. It was shown that these municipalities exist as a result of the South African Constitution (1998). There are three types of municipalities being Category A, B, and C. The responsibilities of each type were discussed. The section indicated the areas in which this study was conducted, and the nature of their environments.

Municipalities do not exist in isolation. The following section discusses those role players who have a direct interest in the running and functioning of municipalities in South Africa and explains further their roles within the municipalities.

3.4 OTHER ROLE-PLAYERS IN THE FUNCTIONING OF MUNICIPALITIES IN SOUTH AFRICA

3.4.1 National Treasury and its role in South African municipalities

The National Treasury is one of the departments within the South African government and is headed by the minister responsible for financial and fiscal matters. The National Treasury must promote the national government's fiscal policy framework and the coordination of macro-economic policy; coordinate inter-governmental relations; manage the budget preparation process; exercise control over annual national budgets; and facilitate the implementation of the annual Division of Revenue Act. Further, it must monitor the implementation of provincial budgets; promote and enforce transparency and effective management in respect of revenue, expenditure, and the assets and liabilities of departments, public entities, and constitutional institutions (Public Finance Management Act, 1999: 9).

This department is expected from time to time to issue circulars and treasury instructions, which guide how municipal finances should be handled. Such circulars and instructions are added to sections in the MFMA, and are issued with the aim of strengthening financial controls within municipalities. The National Treasury is key in ensuring the efficient functioning of municipalities and that they comply with all financial regulation.

3.4.2 Role of Department of Cooperative Governance and Traditional Affairs (COGTA)

As of May 2009, the Department of Provincial and Local Government was changed to the Department of Cooperative Governance and Traditional Affairs (GCIS, 2010: 265). The mandate of this newly formed department was derived from Chapters three and seven of the Constitution of the Republic of South Africa, 1996. The Department of Cooperative Governance and Traditional Affairs (COGTA) has a new and expanded mandate compared to the previous department, which focuses on improving vertical coordination across the three spheres of government and public entities in South Africa; improving horizontal coordination across the various sectors in government and public entities; strengthening, supporting and overseeing provincial governments; improving collaboration between government and communities; and the institution of traditional leadership in a single system of governance (GCIS, 2010: 265).

Therefore, this department oversees all municipal activities, and expects municipalities to report their operations to the department. Its mandate provides for continuous support to ensure that

municipalities run smoothly in tandem with their constitutional mandate, and that they offer all expected services, as detailed above.

3.4.3 Auditor-General South Africa (AGSA)

The Auditor-General South Africa (AGSA) has a constitutional mandate as a Chapter 9 institution to conduct audits and report on the accounts, financial statements and financial management of all national and provincial state departments and administrations, all municipalities, and any other institutions or accounting entities required by national or provincial legislation to be audited (Constitution of South Africa, 1996).

The origin of the authority of the AGSA “derives from the Constitution of the Republic of South Africa (Constitution, 1996). In terms of section 181 of the Constitution (Constitution, 1996), AGSA is a Chapter 9 institution established to strengthen constitutional democracy in the Republic”. Section 188(1) of the Constitution (Constitution, 1996) states that the Auditor-General South Africa must conduct audits and report on the accounts, financial statements, and financial management of:

- “All national and provincial state departments and administrations;
- All municipalities; and
- Any other institution or accounting entity required by national or provincial legislation to be audited by the AGSA”.

This confirms that the independence of the AGSA is imposed by law in South Africa. The operations and powers of the AGSA are also controlled. It could be argued that this regulation adds to responsibility of AGSA in the public service and strengthens democracy in South Africa. The AGSA is, therefore, one of the key players in the running of municipalities in South Africa. The audit comments provided annually by AGSA on its audit reports proved to be important to the way in which the finances of these municipalities are handled over time. It is envisaged that the AGSA will audit these reports and analyse them to determine what improvements can be made with regard to municipalities, and whether there has been any improvement in the running of municipalities from 2008 to 2016.

The AGSA was closely relied upon in this study as it deals directly with the finances of municipalities and directly works and comments on the work performed by the IAFs within all the

municipalities. Therefore, the comments made by this role player were very important to this study as a whole.

3.4.4 The South African Local Government Association (SALGA)

The South African Local Government Association (SALGA) is a listed public entity, established in terms of Section 21 of the Companies Act, 1973 (Act 61 of 1973) and is recognised by the Minister of Cooperative Governance and Traditional Affairs (COGTA) in terms of the Organised Local Government Act, 1997. SALGA represents local government on numerous intergovernmental forums such as the President's Coordinating Council (PCC), the Minister and Members of Executive Council (MECs) forum, and the Budget Forum. SALGA's goal is to achieve the following within municipalities in South Africa:

- To transform local government to enable it to fulfil its developmental role;
- Enhance the role of provincial local government associations as provincial representatives and consultative bodies on local government; raise the profile of local government;
- Ensure full participation of women in local government;
- Act as the national employers' organisation for municipal and provincial member employers; and
- Provide legal assistance to its members, using its discretion regarding matters that affect employee relations (GCIS, 2010: 268).

It is evident that SALGA plays an important role in municipalities in South Africa by ensuring that the municipalities improve and develop their functioning to achieve a high level of maturity which will allow them to fulfil their constitutional mandates successfully.

3.4.5 The Audit Committees (AC)

According to the MFMA (sections 165 & 166) the Audit Committee (AC) functions as an important committee of the municipal council. The AC is expected to perform the functions allocated to it by the MFMA (sections 165 and 166), and the corporate governance responsibilities delegated to it under its charter by the council.

The National Treasury (2001: 2) regards the AC as being an integral part of the process of transparency, accountability, and improved financial management. It is for this reason that audit committees have become a legislative requirement for government. In terms the PFMA, audit

committees are compulsory for national and provincial government departments, as well as for public entities under the control of government, including municipalities of all types. Expanded accountability extends to the sphere of local government, and audit committees have become a legal requirement for all municipalities in terms of the MFMA (Act 56 of 2003).

The AC is seen as an important instrument in the corporate governance of every entity, as perceived by both the PFMA and the MFMA. “The focus on service delivery and accountability in the public sector has increased the focus on good corporate governance. Audit quality and the integrity of financial reports as well as the quality of the system of internal controls in an entity necessitate an independent audit committee that acts as a link between management, internal and external audit” (Van der Nest, Thornhill & De Jager, 2008: 549).

According to Briotta (2004: 12) audit committee members must adhere to high quality standards in corporate accountability to ensure the quality of financial information and of both the internal and external audit processes. Governance in the public sector deserves the same attention given to governance in the private sector. The audit committees in the public sector have similar responsibilities as their counterparts in the private sector. Whereas unethical behaviour in the corporate sector impacts on the shareholders of a company, unethical behaviour in the public sector impacts on all taxpayers and citizens of a country.

The AC’s responsibilities include among others, assisting management by supervising all financial reporting to ensure that it provides truthful and valuable information to users. The King Report (IOD, 2009) states that the AC must “help the board (management, in the case of the public sector) discharge its duties regarding the preparation of accurate financial statements in compliance with all applicable regulations, legislation and applicable accounting standards. When the AC reviews financial statements they must focus on specific issues such as materiality, compliance with accounting policies, significant changes, and areas susceptible to fraud” (PWC, 2006: 3).

The King IV report of 2016 requires that the AC should oversee integrated reporting; ensure that a combined assurance framework is applied to provide a coordinated approach to all assurance activities; satisfy itself of the expertise, resources and experience of the company’s finance function; be responsible for overseeing internal audits; be an integral component of the risk management process; oversee the external audit process and report to council and stakeholders on how it has discharged its duties (IOD, 2016).

In addition to the above requirements of the ACs, the ACs are expected to help the IAFs to perform their functions within their organisations. This recommendation is important to the ACs as they rely on the work of the IAFs, so they always need a value-adding and effective IAF (Van der Nest et al, 2008) indicated the benefits and responsibilities of the ACs as:

- ensuring an independent IAF, which operates efficiently and effectively;
- ensuring that risk management practices are applied in the organisation;
- ensuring that sound corporate governance practices are applied;
- ensuring that the system of internal controls is adequate and functioning effectively; and
- ensuring that fraud and corruption is dealt with effectively” (Van der Nest et al, 2008).

The King IV Report recommended the following responsibilities of the AC regarding IAFs: the AC should play a key role in ensuring that the company’s IAF is independent and has the necessary resources, standing and authority within the company to enable it to discharge its functions.

Therefore, the ACs are seen as important role-players in the functioning of the IAFs, and their powers and roles can lead to the proper functioning and effective IAFs. The relationship between the AC and IAF is central in enabling the AC to meet its responsibilities. The question remains as to whether the ACs are provided with the required services by the IAFs, thus facilitating the work of the ACs and enabling them to render their oversight role effectively.

Summary

The above discussion considered various role players in the functioning of municipalities in South Africa such as the National Treasury Department, the Department of Cooperative Governance, and Traditional Affairs (COGTA), AGSA, SALGA and audit committees (ACs). It was evident that each of the role players discussed has a special interest and role to play in the functioning of municipalities in South Africa, to ensure that the constitutional mandates of the municipalities are achieved.

3.5 CONCLUSION

This chapter examined the various laws and legislations that shape the IAFs in local government in South Africa. which included: the ISPPA (standards) with special focus on performance standards, the MFMA looking at the requirements, Municipal Systems Act of 2000 which all municipalities must comply with, Municipal Structures Act of 1998, the Municipal Property Rates Act of 2004, the

National Treasury regulations and the AGSA. These laws and regulations provide clear guidance on how the municipalities need to function in order to be value-adding and effective. However, whether these laws and regulations as promulgated, applied and used in South Africa are indeed followed by the existing municipalities is still to be established.

Further discussion on the municipalities in South Africa included the types of municipalities that can be formed, and a list of the existing municipalities in different provinces within South Africa. This discussion was important as it provided a background on the types of municipalities that can be established and what roles each type plays in the country. The chapter considered other role-players in the functioning of the municipalities in South Africa such as the National Treasury Department, the Department of Cooperative Governance and Traditional Affairs (COGTA), the AGSA, SALGA, and the AC. These role players were found to have direct interest in the running of municipalities, and to play a special role in their existence. These role-players provide guidance and supporting functions to municipalities with the aim of ensuring that the municipalities become efficient and deliver on their required and expected mandates.

Based on the discussion made in this chapter it is clear there are various laws and regulations which govern the running and functioning of municipalities in South Africa to make them the functioning municipalities and there are different types of municipalities existing in South Africa which are expected to run as per laws and regulations stated above.

The following chapter (Chapter 4) discusses the various views of researchers on the effectiveness of IAFs, and examines various studies performed in other countries and areas on the effectiveness of IAFs.

CHAPTER 4

THE EFFECTIVENESS OF IAFS

4.1 INTRODUCTION

The effectiveness of any function in any organisation is seen as an important tool that makes and proves the existence of such a function. The word 'effectiveness' is defined by different researchers such as Arena and Azzone (2009: 11) as the ability to obtain the anticipated outcomes that are in line with the stated objectives. Thus, effectiveness became a cornerstone of this study, which aimed at assessing the effectiveness of IAFs in South African municipalities. The chapter examines the views shared by researchers and authors from other countries on the effectiveness of IAFs, and explains the meaning of the concept of effectiveness as applied in this study.

This chapter looks at various views shared by different researchers on the effectiveness of IAFs in different organisations in different countries. This chapter attempts to discuss what other research found on the effectiveness of IAF and identifies the gaps that other research already conducted lacked in their research. The chapter further aimed at determining the accepted bases for measuring the effectiveness of IAF in different countries.

This chapter focuses on the following: discusses different views the researchers have on the effectiveness of internal auditing, which indicates how different sources view the effectiveness of IAFs. This is followed by a presentation of other researchers' work on the effectiveness of internal audits, and the areas that they focused on. The prescriptions of the Municipal Finance Management Act (MFMA) are then examined in terms of the requirements of the Act.

The following section discusses the importance of the IAFs within organisations, including municipalities.

4.2 IMPORTANCE OF THE IAF

The importance of an effective IAF is proved in the growing need for this service in all organisations across the board, and in the rapid growth of its professional organisation (IIA, 2010). However, despite the rapid growth of IAFs, researchers have paid little attention to this function and its importance. While its use is not questioned, its contribution has not been measured scientifically (Eden & Moriah 1996).

According to Cohen and Sayag (2010: 1) internal auditing "has become an essential control tool available in both public and private organisations, yet very few academic studies have been conducted on the effectiveness of internal audits within organisations". The effectiveness of

internal auditing is “worthy of attention because internal auditors are important, even crucial, in an economy that relies upon independently produced information” (Van Peurseem, 2005). Indeed, the IAF has become a crucial management tool for accomplishing effective control in both public and private organisations (Eden & Moriah 1996). Control mechanisms “are those processes set up to monitor and direct, promote, or confine the various activities of an enterprise in achieving its objectives” (Sawyer 1988; Coram, Ferguson & Moroney, 2008). In recent years, the IAF has become a key corporate governance mechanism alongside audit committees, external audits, and management (Cohen, Krishnamoorthy & Wright, 2004; Gramling, Maletta, Schneider & Church, 2004; Schneider, 2009). As reflected in the Institute of Internal Auditors’ (IIA, 2009), “internal auditing is an assurance and consulting activity concerned with evaluating and improving the effectiveness of risk management, control, and governance processes.

By detecting deficiencies in management operations, the IAF provides a basis for correcting deficiencies that have eluded the first line of defence before they become uncontrollable or are exposed in the external auditor’s report (Eden & Moriah 1996). As an example, Coram et al. (2008) found in a sample of 324 Australian and New Zealand organisations that those with an IAF were more likely to detect and self-report fraud through misappropriation of assets than those who did not have this function in their organisations.

Albrecht, Howe, Schueler and Stocks (1988), in a study supported by the Institute of Internal Auditors (IIA), identified 15 criteria used by 13 large private organisations to evaluate the effectiveness of an IAF. They concluded that effectiveness is “determined mainly by the fit between the auditing work and the goals set by managers, the qualifications of the internal auditor, management support for the internal auditing staff, and several characteristics of the internal auditing department. Lampe and Sutton (1994) identified 15 factors that contribute to an effective audit, and categorised them into three stages of the auditing process, namely, planning, fieldwork, reporting and review. They suggested measurements they considered valid and reliable for these factors. Thereafter, Ziegenfuss (2000) developed a questionnaire that included 84 criteria for effectiveness, categorised into four main areas: the environment of the internal audit, input into the audit, the auditing process, and the output of the audit.

4.3 VIEWS ON EFFECTIVENESS OF THE IAF

The word effectiveness has been defined by different researchers such as Arena & Azzone (2009:11) “as the ability to obtain expected results that are in line with stated objectives while Dittenhofer (2001: 41) viewed effectiveness as one’s capacity to accomplish specified objectives

and goals. Mihret and Yismaw (2007: 6) expanded on this definition by stating that internal audit effectiveness means the extent to which an IAF meets its purpose". This means that effectiveness is measured in terms of ability to achieve the stated objectives and goals.

Al-Twaijry, Brierley and Gwilliam (2003: 1) in their study titled "The Journey so far on Internal Audit Effectiveness", concluded that audit effectiveness is the result of internal auditors' activities, duties, professional practices, and responsibilities through a high commitment to audit standards, goals, objectives, policies, and procedures. The researcher of this study shares the same understanding outlined above, and in summary, views effectiveness as the ability of a municipality to achieve its stated objectives and goals.

Previously conducted research was found to differ vastly in determining and measuring the effectiveness of IAFs, as some researchers looked at different areas when determining the effectiveness. Some examples of such areas are explored below.

Mihret and Yismaw (2007: 15) studied the effectiveness of internal audit in public sector higher educational institutions in Ethiopia. The study identified four factors that impacted on the effectiveness of IAF as: "internal audit quality, management support, organisation setting, and auditee attributes. The results of this study found that the IAF was not effective in terms of proficiency, planning, recommendations, and limitations on the scope of the work". The authors suggested a need for future research to fully understand the effectiveness of IAFs in the public sector by identifying other variables affecting internal audit effectiveness other than the ones explored in their study.

Yee, Sujana and James (2007: 12) conducted the study on the perceptions of the Singaporean managerial class regarding the role and effectiveness of internal audits in Singapore. They studied the perceptions of Singapore's managers including those in senior, middle, and junior management regarding the role and effectiveness of the IAF. In contrast to the Saudi Arabian (Al-Twaijry et al. 2003) and Ethiopian (Mihret & Yismaw 2007) findings, the overall findings of Yee et al. (2007) were as follows: 1) the IAF in Singapore is improving and has become an important part of organisational structure as a value-adding service 2) In general, managers are satisfied with the services provided by their IAFs. Yee et al. (2007) recommended a need to explore the role and effectiveness of IAFs in developing countries such as the Middle East and Africa, because in developing countries, IAFs can ensure that capital is not wasted through inefficiency, fraud, and corruption.

The study by (Al-Twaijry et al., (2003) on the other hand, used major elements of SPPIA to measure the effectiveness of IAFs. The results of the study suggested "that the level of internal

audit effectiveness differed amongst organisations. According to the study, the IAFs authority and responsibility and its link with senior management, are the most important factors for improving the effectiveness of IAF. The authors concluded their study by suggesting that internal audit effectiveness in the private and public sectors need to be looked at separately in order to produce useful insights, as their operational approaches differ.

Arena and Azzone (2009) in their study, considered the organisational drivers of internal audit effectiveness in Italian companies. The study results suggested that “the role of IAF had increased because of IAF links to the internal control-risk management system. Their study defined a framework to measure internal audit effectiveness as a dependent variable; the resources and competencies of an internal audit team, the audit processes and activities; and the level of interaction between the IAF and the audit committee as independent variables”. The results of their study concluded that internal auditors need to develop new skills to perform activities that are more related to risk management, which requires internal auditors who are able to deal with different sources of risk and to increase managers’ confidence in risks and controls. The results of their study also explained that internal audit effectiveness is influenced by the characteristics of the IAF, the audit processes, activities, and organisational links. Arena and Azzone (2009) further stated that:

“Internal audit effectiveness increases in particular when the ratio between the number of internal auditors and employees grows, the CAE is affiliated to the Institute of Internal Auditors, the company adopts control risk self-assessment techniques, and the audit committee is involved in the activities of the internal auditors”.

The study highlighted that there is a need for more detailed analysis on internal auditors’ competencies in order to understand which specific skills influence their work.

Goodwin (2004: 646) made a comparison between the role of IAF in the government sector and those in the private sector in both Australia and New Zealand. The author highlighted that there “was no requirement for private sector organisations in Australia and New Zealand to establish an IAF. However, the Australian Stock Exchange encourages only large companies to have an IAF to comply with listing requirements”. It was not clear whether such requirement exists for the public sector, as the public sector organisations and entities’ compliance in Australia depended on the specific legislation governing such an organisation or entity. On the other hand, the public sector in New Zealand had no requirement for an IAF.

According to Savcus (2007:280) there is close relationship between the value adding role of the IAF and its effectiveness. Savcus (2007: 281- 282) continues to suggest the following qualities for

the IAF's effectiveness, namely: subordination to the audit committee, professional certification, experience, internal audit strategy and operating responsibilities. Coram, Ferguson and Moroney (2008: 546) acknowledge that there has been limited research on the effectiveness of IAFs, which warranted this study. Arena and Azzone (2009: 44) linked the effectiveness of an IAF to the resources and competencies of the internal audit team, activities and processes performed and its organisational role.

The above studies conducted on the effectiveness of internal audit differed broadly on the determinants that make the IAF effective. Therefore, the study considered the effectiveness of IAFs in South African municipalities as perceived by the stakeholders in those municipalities. The researcher is of the view that the stakeholders found in these municipalities have sound and sufficient knowledge to indicate whether their IAFs are effective or not, and whether they provide the value required.

In the South African context and the context of this study, the above discussion is strengthened by section 165 of the Municipal Finance Management Act (MFMA), which emphasises the role of the IAF (referred to as the internal audit unit), by stating that the IAF of a municipality must prepare a risk-based audit plan and an internal audit programme for each financial year as required by the IIA standards, and advise the accounting officer and report 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 this Act, the annual Division of Revenue Act and any other applicable legislation.

Section 165 of the MFMA as indicated above prescribes the establishment of IAFs as they are important components of internal control, risk management and corporate governance, and provide the necessary assurance and advisory services to an organisation. The IAF is one of the most significant management tools, and can provide value-added services to municipalities. When objectively and adequately resourced, the IAF should be in a position to provide management with assurance regarding the effectiveness of the systems of internal control, risk management and governance processes.

To achieve the effectiveness mentioned above, the International Standards for the Professional Practice of Internal Auditing (IIA Standards, 2013) states that "the relationship between the IAF and the audit committee should be such that the CAE functionally reports to the audit committee (representing a level within the organisation that allows the IAF to fulfil its responsibilities) and that

the IAF should provide the committee with appropriate information” (IIA 2013 Practice Advisory, 1110-1).

Turley and Zaman (2004: 309) “believe the latter relationship strengthens the IAF, which, according to Gramling, Maletta, Schneider and Church (2004: 198), increases the standing of the IAF within an organisation. Sarens, De Beelde and Everaert (2009: 91), who studied the reason why audit committees look to the IAF for support, found that audit committees seek relaxation with respect to the control environment and internal controls, and that the IAF can provide such a relaxation. This raises the question on whether the IAF within municipalities in South Africa provides audit committees with such comfort that the audit committees can rely on”. This indicates another focal point covered by the study.

The above paragraphs are supported by Grafenstine (2014: 13) who claimed that “IAFs which do not understand their organisational environment provide limited value, damage trust, and fail to make meaningful change within their own organisations”. Grafenstine (2014) further commented that in order to add value and reduce risk, the IAFs need to be proactive, understand their organisational operations, strategy, goals and objectives, and risk appetite. This is expected in the case of IAFs in the public sector as well, in order for them to remain effective and add the required value to their municipalities.

Based on the above definitions and discussion on the effectiveness of IAFs, this study defined internal audit effectiveness as the ability of IAFs to assist the management of municipalities in achieving the established objectives within the municipalities in South Africa.

4.3.1 Summary

The IAF has grown from a traditional function focused on detecting risk areas, to becoming a value-adding function to organisations. For IAFs to be value-adding, they must be effective. Therefore, prior research suggests that it is important for organisations to measure the effectiveness of IAF to ensure that it provides the value required by the organisation. However, the research findings indicated above have shown that the IAF may not always be effective in organisations, due to the various reasons drawn above. Prior research has shown that the role of the IAF differs between the private and government sectors. It appears that there is a gap in previous research regarding the examination of the effectiveness of IAFs, as studies utilised different criteria to determine the IAFs e effectiveness. Further noted from prior research is that it focused on the effectiveness of IAFs in mixed sectors (government and private sectors) and used different research theories. Therefore, as most of the prior research indicated, there is a great need

for future research to examine the effectiveness of the IAF and clearly show the determinants that make IAFs effective. This can be best realised if the stakeholders themselves, who rely on the work of these IAFs, can clearly indicate the effectiveness of their IAFs and specify what they require of the IAFs to fully satisfy their expectations. The study bridged this identified gap that exists in the literature.

The following section discusses the findings of different studies conducted on the effectiveness of the IAFs from 2011 to the present.

4.4 STUDIES ON IAF EFFECTIVENESS FROM 2011 – 2016

This section presents the findings of other research/studies have found on the effectiveness of IAFs.

Dittenhofer (2001: 444) stated in his study on internal auditing effectiveness that an expansion of present methods found that internal audit effectiveness can be determined by evaluating the quality of internal auditing procedures. This study by Dittenhofer, placed its focus on the internal audit procedures that are conducted by the IAF and suggests that the internal audit effectiveness will be greater if quality audit procedures are conducted. This study suggests that the IAF needs to conduct internal audits based on informed facts and information that is considered effective by those in authority. Among other things, this study determined what auditing procedures are conducted within South African municipalities to ensure the effectiveness of IAFs.

Dhamankar and Khandewale (2003: 275) in their study on the effectiveness of IAFs, found that it was “generally accepted by the study participants that the IAF is an important component of good corporate governance, and that an effective IAF would be a strong tool for any management team”. This idea encouraged the researcher to determine, from the municipal participants’ point of view, their opinions on their own IAFs.

A paper presented at a New Delhi (2006: 37) seminar on improving the effectiveness of the IAF in Indian government departments, found “the use of IAFs in its Union Ministries and other departments to be an uncertain area requiring immediate attention for greater functional clarity”. Along similar lines, this study attempted to ascertain if the effectiveness of IAFs in South African municipalities is truly effective and functioning as expected.

Belay (2007: 6) in his study on effective implementation of the IAF to promote good governance in the public sector in Ethiopia, indicated that the existing IAFs in the public sector show little evidence of IAF effectiveness in governance structures, due to lack of resources, poor leadership,

and lack of suitable frameworks to measure IAF performance. The researcher intends to determine the effectiveness of the IAFs in South African municipalities, and the reasons and challenges attached thereto.

Mizrahi and Ness-Weisman (2007: 191) in their study based on evaluating the effectiveness of auditing in local municipalities in Israel, used an analytic hierarchy process and a general framework. It was established in this study that “the effectiveness of IAFs in Israeli municipalities is low.

Kuta (2008: 21) in his study on the effectiveness of IA for proper accountability in Nigerian local governments, found that IAFs in Nigeria’s local governments are ineffective. According to the study, factors responsible for this included “lack of independence of the IAF, no programmed preparation, insufficient funds, understaffing, and that the IAF reports are given little credibility.

Yee, James and Leung (2008: 147) in their study on perceptions of Singaporean internal audit customers regarding the role and effectiveness of the IAF, found that both Singaporean senior and junior managers appreciate the professionalism and effectiveness of the IAFs that serve their businesses. This study is one of the few that showed positive results regarding the effectiveness of IAFs.

Ahmad, Othman and Jusoff (2009: 784) in their study on the effectiveness of internal audit in the Malaysian public sector pointed out that that a lack of appropriate internal audit staff members is ranked as the main challenge facing IAFs when conducting effective internal audits.

Bota-Avram and Palfi, (2009: 784) in their study on measuring and assessing the effectiveness of internal audits, indicated that for organisations, including government organisations, it is important to find the most relevant and applicable methods to measure and assess the effectiveness of the IAFs.

In their study, Unegbu and Kida (2011: 306) on the effectiveness of internal auditing as an Instrument of improving public sector management revealed that the IAF, if properly utilised, can effectively assist in fraud detection and other fraudulent activities in the public sector, and thus safeguard the resources of organisations.

Summary

The literature review above shows some of the various studies conducted on the effectiveness of internal auditors that were examined by the researcher in the course of reviewing the available literature. However, it was found that all the above-mentioned studies focused on different factors or criteria when looking at the effectiveness of IAFs. Therefore, this study specifically considered the effectiveness of IAFs in South African municipalities to assist future research in this area.

4.5 FRAMEWORKS DEVELOPED BY OTHERS IN INTERNAL AUDITING

Due to differences in organisations and their aims, the “one fits all” approach is not practical, and for this reason, many researchers develop various frameworks to bridge the existing gaps in the generic frameworks recommended by the IIA. These frameworks are now discussed:

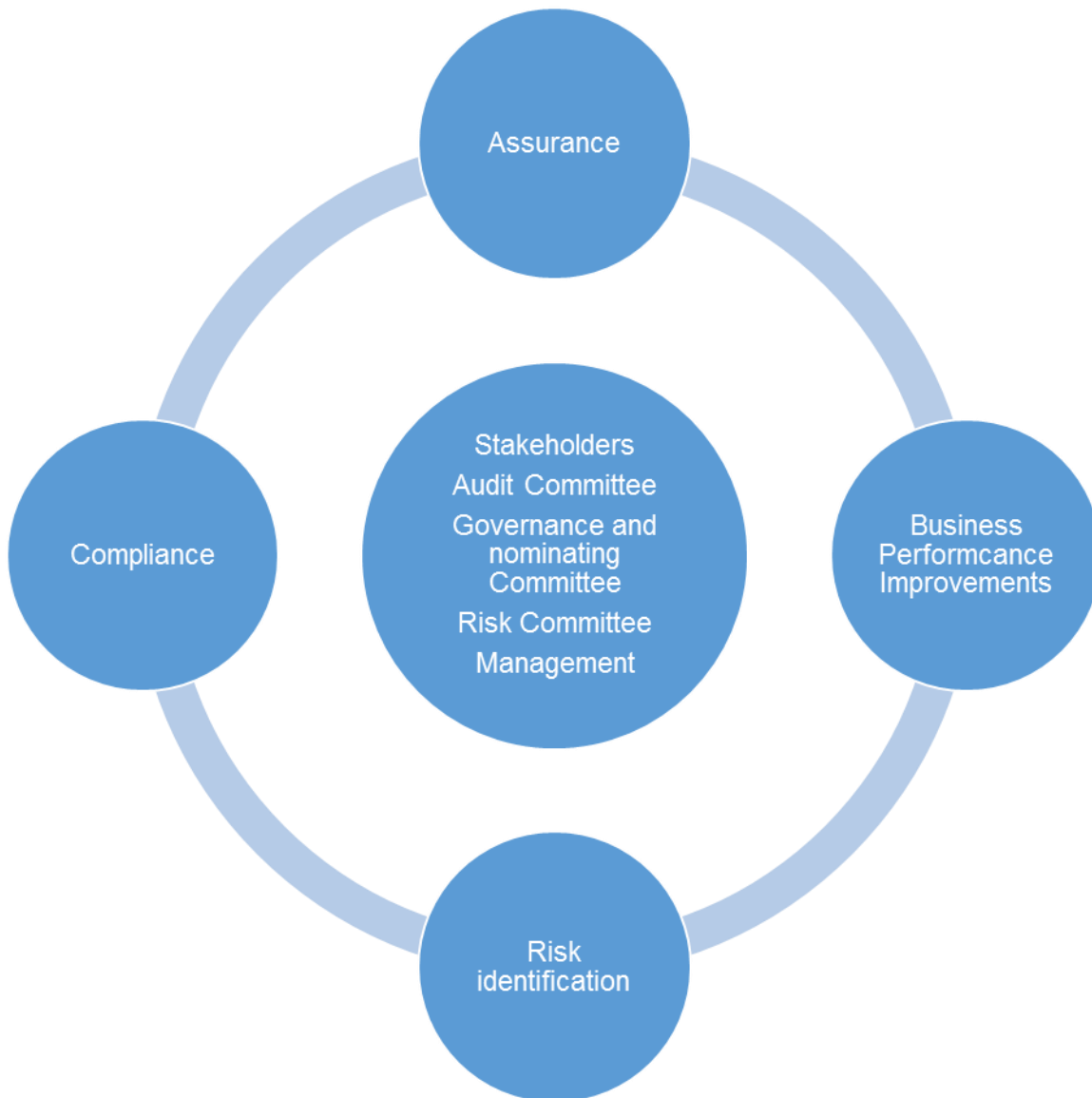
The Chartered Institute of Internal Auditors developed the framework below for an effective IAF (Peters, 2015):

1. Excellent knowledge of the organisation and the sector(s) and markets in which it operates.
2. Specialist knowledge and expertise to provide a wider range of assurance e.g. in the areas of IT, project management, treasury, customer relationships, contracts, etc.
3. Flexibility and responsiveness to emerging risks and issues.
4. Confidence and trust of senior management to be involved in major projects and change.
5. Independence and objectivity.
6. Risk based internal audit planning and an agreed audit methodology
7. Providing advice and guidance to support organisational objectives through consultancy.
8. Consistent levels of service delivery.
9. Coordination and collaboration with other assurance providers.
10. Effective teamwork.
11. Career development opportunities within the IAF or the wider organisation.
12. Commitment to quality and continuous improvement.

According to this framework, an effective IAF needs to follow and strive for all the points indicated. However, it must be noted that the framework does not take into account other elements of IAF that contribute to the effective IAF, such as the independence of the IAF. The framework is also too generic and does not provide a special focus on the IAF expected in a municipality functioning in South Africa. Therefore, this framework does not provide all the answers for an effective IAF of a municipality.

The New Internal Audit Framework developed by Crowe Horwath (2010) is based on the four main principles that govern the effective IAF:

Figure 4.1: Crowe Horwath's new Internal Audit Framework



Source: Crowe Horwath's New Internal Audit Framework, 2010

This framework is explained as follows:

Compliance:

The first principle of this framework is compliance. Compliance audits are explained as testing past events and transactions to determine whether previous actions are in compliance with policies and procedures, laws, and regulations. With this framework the IAF keeps a record of applicable compliance mandates and other legal and regulatory requirements, and monitors the processes that manage compliance using the Sarbanes-Oxley Act (SOX), an Act which was promulgated in the United States in 2002. Using the new framework, internal auditors rely on the work of business unit managers and the reports that managers use to monitor controls in their units, as a starting point for the audit. Only those issues that are red-flagged during the audit of the control processes are then homed in on for further investigation. Auditors can use reports from various business units generated within; for example, from the information technology department, to determine whether the control processes that are in place safeguard security sufficiently and provide for an appropriate segregation of duties. Similarly, internal auditors can continuously review control reports to confirm that processes are in place for timely reconciliation. If management checks sample transactions each month, the internal auditor does not need to do the same checks; rather, he or she needs simply to verify that management is doing what is needed.

Business performance improvements:

According to this framework the internal auditors' continuous appraisals of business processes for effectiveness and efficiency can lead to better-quality business. In the past, when auditors identified problems they might not have taken the extra step to recommend ways to improve them and thus raise business performance. Many of the control reports auditors collect can be considered as benchmarks or best practice. This type of analysis can show that a company may be taking twice as long to perform an operating procedure as its peers, or that a company should add people to attain higher productivity. With this knowledge, changes can be made that add value to the organisation as a whole.

Assurance:

For up-to-the-minute testing, continuous monitoring systems must be in place to oversee events, transactions, and results, and to generate reports that highlight early warning signs that something is outside the bounds of tolerance. By regularly analysing and reviewing control reports generated by a system, auditors can provide a level of continuous assurance that supports stakeholder confidence that everything is under control at all times.

These real-time reports keep present events from becoming out-of-control problems. If expenses in a certain business unit are out of line or should not have been approved for example, the continuous monitoring systems at the business-unit level should flash a warning or automatically send an e-mail to the appropriate person. The same system might also indicate the accounts of customers who have previously failed to pay, so that no new sales are made to defaulting customers. Although there is the up-front cost of installing a continuous monitoring system, it eliminates the need for auditors or staff to perform these monitoring tasks manually. The time saved allows auditors to focus on other important matters.

Risk Identification:

This framework recommends that the future risks need to be identified and understood timeously so that they do not prevent a company from accomplishing its business objectives. The framework further indicates that the key risks are always changing. By applying continuous monitoring and appraisal methods, internal auditors make the process of identifying and managing risk more reliable and resilient. A number of different groups in a company are likely to be performing risk-management activities for compliance or safety purposes, for example. Here again, internal auditors can use their time efficiently by using the existing assessments of each of these groups to increase stakeholders' knowledge of the risk environment. Thus, the risk assessment process for the organisation becomes more integrated. To evaluate emerging risks, internal auditors can review the processes various groups in the company already use for emerging risk evaluation. For example, a company developing a new product, has in place a process for estimating the return on investment (ROI) for that product. The risk to the company is that the projected ROI of the new product is not yet realised. Internal audit can review and monitor reports on the process the product development group uses, to determine the ROI expected for the new product.

This framework identified important principles that can be used in IAFs to comply, assure, identify risks, and improve performance within organisations. However, this is a framework suitable for use in profit-making organisations. And does not fit non-profit organisations or the public sector environment. Therefore, there is need for a municipality-specific framework that takes into account the environment under which municipalities in South Africa operate.

4.6 DETERMINANTS OF EFFECTIVENESS OF IAF

The most important people to judge the effectiveness of IAFs are the staff to whom the IAF service is being rendered. For the purpose of this study, this refers to the municipal managers, accounting officers, mayors, and staff in general. The study looked at the views of these stakeholders through the AGSA reports to find out if they consider their IAFs to be effective, and if so, what informs them to make such a conclusion. If the IAFs are not considered effective, there must be a plan made to make these functions effective and value-adding. The following discussion looks at what determines effective IAFs according to the available literature.

4.6.1 Organisational independence

The role of the IAF in organisations is more complex, whether looked at from the private or public sectors' point of view. Van Peurseem (2004: 378) highlights that there is a strong possibility for confusion in the relationship between internal auditors and management, as internal auditors are likely to assist those in authority within their organisations in doing their daily duties and at the same time to independently evaluate management's effectiveness. Internal auditors are charged with upholding the best interests of their authorities, but they may be reluctant to act counter to management, regardless of the results. This could lead to a self-review threat in the sense that internal auditors might be seen as evaluators of their own work.

Bou-Raad (2000: 185) argued that the strength of an IAF must be measured with respect to the level of independence it enjoys from senior management and from functioning responsibilities. The IIA, the American Institute of Certified Public Accountants (AICPA), and other professional bodies have identified organisational independence as critical to the sustainability of the IAF (Brown 1983: 444). Internal auditors should be sufficiently independent from their clients that they can both conduct their work without any interference and equally important, should be seen to do so. Coupled with objectivity, organisational independence contributes to the accuracy of the internal auditors' work and gives managers confidence that they can rely on the results and the audit report produced.

In support of the above, Schneider (2010: 19) argues in his study on assessment of internal auditing by audit committees, that the independence of internal auditors is: a critical aspect of the IAF and standards set forth by the Institute of Internal Auditors (IIA), and International Standards for the Professional Practice of Internal Auditing, define internal auditing as an independent assurance function and require internal auditors to be autonomous from activities they audit.

Schneider's study is in agreement with the IIA (Standard 1100), which states that the IAF must be independent and internal auditors must be impartial in performing their work. This Standard interprets and explains the independence of internal auditors as follows:

“Independence is the freedom from conditions that threaten the ability of the IAF or the CAE to carry out internal audit responsibilities in an impartial manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the chief audit executive has direct and unrestricted access to senior management and the board. This can be achieved through a dual-reporting relationship. Threats to independence must be managed at the individual auditor, engagement, functional and organisational levels. Objectivity is an unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others”.

The IIA standard 1110 regarding organisational independence states that:

“The CEO must report to a level within the organisation that allows the IAF to fulfil its responsibilities. The CEO must confirm to the board, at least annually, the organisational independence of the IAF. The IAF must be free from interference in determining the scope of internal auditing, performing work, and communicating results. Internal auditing will report to the highest level of management and be free of any other operating responsibility. This is further supported by ISA 610 of the International Federation of Accountants (IFAC: 1994)”.

Based on interviews with Australian internal auditors, Van Peurse (2005: 489) concluded that independence from management is the main feature of successful and effective audit functions in any organisation. Therefore, it could be argued that higher organisational independence is related to higher auditing effectiveness. If the IAF is independent from its management, it can provide this effectiveness and add the required value.

4.6.2 Senior management support

The literature offers sufficient evidence that key to the success of almost all IAFs and processes within any organisation, is senior management support. Based on their study, Fernandez and

Rainey (2006: 169) argued that senior management's support and commitment to change play a crucial role in organisational renewal, as senior managers can organise the critical resources needed to follow through on efforts launched by one or two visionary thinkers. Several empirical studies found that senior management support of quality is a key factor to its improvement. Senior managers' attitudes and behaviours were also been found to be directly related to quality management practices by Flynn, Schroeder and Sakakibara (1994: 339). Takeuchi's (1981) survey of companies with high-quality performance found that 89% of companies had CEOs who frequently visited the factory floor, participated in training programmes, and attended company-wide quality-improvement events.

An IAF must be sufficiently well resourced to recruit and retain the right number of high-quality internal auditors, to keep up-to-date in training and development, "to acquire and maintain physical resources such as computers, and so on. In a survey conducted on Australian internal auditors, Leung, Cooper and Robertson (2004) found that CEOs are generally very positive about the performance of IAFs. They consider IAF members as an essential part of the management team and believe that they can influence decisions, maintain sufficient levels of objectivity, integrity, and competence in their jobs, and provide good support to their own staff. More importantly, they view the support of senior management as a key factor in ensuring the effectiveness of their role. Sarens and De Beelde (2006: 64) reported on the development of a similar attitude in Belgium, where, as a result of recent changes in national and international corporate governance regulations, the IAFs now get more attention and support from boards, managers, and those in authority". The stronger senior management support, the higher the IAF effectiveness.

In conclusion, it should be stated that while IAFs should be independent from management, they need managerial support for their ongoing existence. It is paradoxical that the operation of IAFs in organisations should be independent from management, but need management to support the importance and existence of IAFs. Furthermore, internal auditors cannot be independent to the same extent as external auditors, because they are employed by the organisations they serve. They should, however, be independent from other functions in the organisation in order to continue adding value.

4.6.3 Quality of audit work

According to Glazer and Jaenike (2001), "performing audit work according to internal auditing standards contributes meaningfully to the effectiveness of the IAF. Ridley and D'Silva (2007) found in their study conducted in UK, that complying with professional standards is the most important

contributor to IAFs' value adding role. Standards for audits and audit-related services are published by the IIA (2015) and include attribute, performance, and implementation standards. In general, formal auditing standards recognise that internal auditors should also provide services regarding information other than financial reports". They require internal auditors to perform their roles objectively and in compliance with accepted criteria for professional practice, such that the internal audit assesses and contributes to the enhancement of risk management, control, and governance, using a systematic and disciplined approach. This is important not only for compliance with legal requirements, but because the scope of an auditor's duties involves the evaluation of areas in which a high level of judgement is involved, and audit reports may have a direct impact on the decisions or the course of action adopted by management (Bou-Raad 2000). It can thus be argued that effectiveness is improved through high-quality IAF's work done in compliance with formal standards, and high levels of efficiency in the audit's planning and execution.

4.6.4 Professional proficiency of internal auditors

Appropriate staffing of the IAFs combined with good management of such staff are key to the effective operation of an IAF. An audit requires a professional internal auditor who possesses the necessary education, training, experience, and professional qualifications to conduct the full range of audits required by its audit directive (Al-Twaijry, Brierley & Gwillian 2008: 507). Auditors must comply with the minimum on-going education requirements and professional standards published by their relevant professional organisations and the IIA (2015). Bou-Raad (2000) argued that internal auditors must have high levels of education in order to be considered a human resource. The variety of skills required, according to Bou-Raad (2000), represents a major challenge to professional bodies, tertiary institutions, and management. The few studies that have considered this issue found that the greater the professional qualifications of the internal auditors in a given IAF (defined by the duration of their professional training and educational level), the greater the effectiveness of the IAF (Albrecht, Howe, Schueler & Stocks 1998; Ratliff 2006). It can be concluded that the higher the professional expertise of the internal auditors in the IAF, the higher the auditing effectiveness.

The above discussion looked into various determinants indicated in the available literature that have a bearing on the effectiveness of an IAF, such as senior management support the organisational independence of the IAF, the professional proficiency of the internal auditors, and the quality of their work.

This study considered the main determinants of effective IAF in municipalities in South Africa from a stakeholder's perspective. The Auditor-General South Africa (AGSA) reports from 2008 to 2016 were analysed to determine what the AGSA identified as the determinants of effective IAF.

The following section discusses the specific methods recommended in the literature that can be employed to measure the effectiveness of IAFs.

4.7 METHODS OF MEASURING THE EFFECTIVENESS OF IAFS

A study by Stefanescu, Popa and Bota-Avram (2009: 1) suggests that IAFs face the challenge of having to prove their effectiveness within their organisations, meaning that IAFs intend to eliminate the unpleasant label of being "resources consumer" to become "providers of value-adding services". In this context, the problem of measuring and evaluating the performance of IAFs attracts the attention of both internal auditors and those who follow and use the results of internal audit work. The ISPPA states that: "The CEO must develop and maintain a quality assurance and improvement program that covers all aspects of the IAF" (1300- Quality Assurance and Improvement Program) (IIA, 2014). According to the interpretation offered by the new version of internal audit standards issued by The Institute of Internal Auditors in 2008 and applicable in 2009, "this program also assesses the efficiency and effectiveness of the IAF and identifies opportunities for improvement". This interpretation is in line with this study's intended purpose of examining the effectiveness of IAFs in municipalities in South Africa.

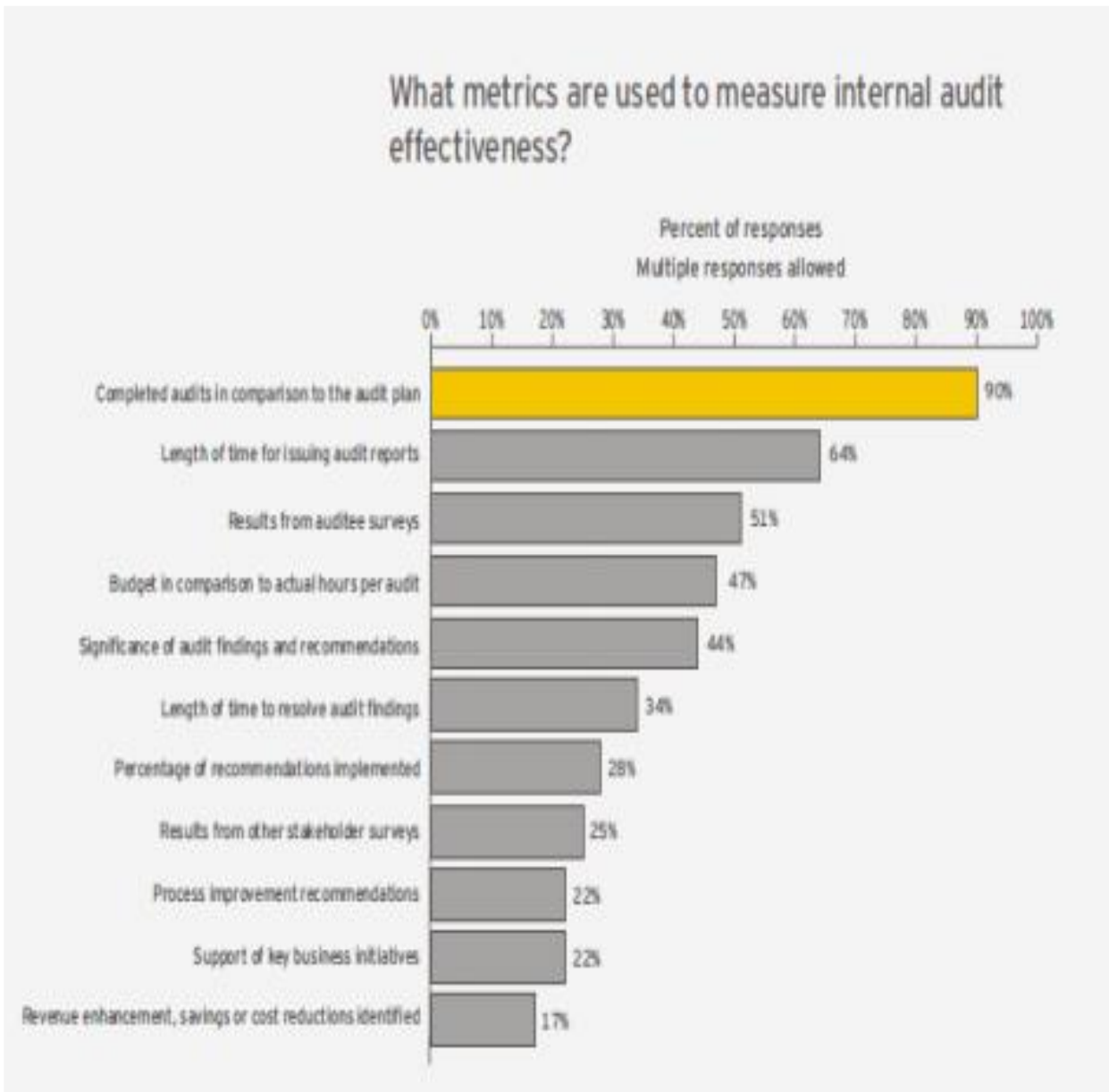
Studies conducted by Deloitte, (2010); PricewaterhouseCoopers, (2010); Pop and Boța-Avram, (2009) suggest that there is a necessity to re-consider the strategy of the IAF, or to rethink a new framework of IAF. One of recent key trends identified internationally indicates that the auditing world is currently confronted with growing interest in the measuring and evaluating of the performance of IAFs. This leads to a necessity to choose reliable methods to assist in detecting the real level of performance achieved by IAFs within organisations, both quantitatively and qualitatively. It has thus become necessary to periodically organise, under an audit committee's supervision, the external evaluation of the level of performance of IAFs, determined by the internal audit itself.

Deloitte, (2010); PricewaterhouseCoopers, (2010); Pop and Boța-Avram, (2009) further suggest that current views on the IAF show a strong concern for value-added provided by internal auditors within their organisations worldwide, and also in the methods used to reliably evaluate and measure the effectiveness of internal audits. The challenges in "measuring the effectiveness of

IAFs is receiving increasingly significant attention, prompting internal auditors to face the significant challenge of finding the best and relevant metrics for measuring the efficiency and performance of their function, and for quantifying the progress made in achieving its goals and objectives (Prawitt, 2003)". The difficult economic context requires accurate answers to questions such as: Of the methods used for measuring the IAF's performance, which methods are more relevant and more effective?

Ernst & Young, being one of the big four global audit firms, conducted relevant studies focusing on international audit practices, with the results being incorporated in the "Global Internal Audit Survey". In 2008, a study was conducted on internal audit executives representing 138 mainly public companies drawn from Global Business Week 1000 and Standard & Poor's Global 1200, Most of the participants' companies (in 24 countries) were large multinationals with revenues of over US\$ 4 billion. Ernest & Young found that "half of the respondents (50%) did not track the value of the IAFs provided to their organisations, while only 13% measured value based upon actual cost savings. The importance of value tracking is demonstrated by the fact that it reinforces the IAF's relevance as well as helping to justify the investment in resources necessary for the IAF. Regarding the methods used for evaluating IAFs' performance, the survey (Ernst & Young, 2008) showed the most-used methods for measuring effectiveness". These are shown in Figure 4.2 below.

Figure 4.2: Metrics used in measuring internal audit effectiveness:



Source: Ernst & Young, 2008

Regarding methods used for evaluating the IAFs' performance as shown in Figure 4.2 (Ernst & Young, 2008) demonstrates that the most-used methods for measuring internal audit's effectiveness are:

- Completed internal audits in comparison to the internal audit plan (90%);
- The length of time taken for issuing internal audit reports (64%);
- Only 32% of respondents used length of time to resolve internal audit findings as a key metric, and

- 23% used support of key business initiatives.

Arena and Azzone (2009: 43) conducted a study aimed at understanding the organisational drivers of internal audit effectiveness, taking into account the recent changes in the field of internal audit, and its main role in corporate governance. The data used for their study were collected through a questionnaire, which was sent to 364 Italian companies. A response rate of 47% was obtained. Based on data from 153 Italian companies, the Arena and Azzone (2009: 43) survey revealed that the effectiveness of IAF is influenced by factors such as:

- What characterises the internal audit team;
- the audit procedures and activities followed; and
- the links the organisation has.

The study further revealed that there is an increasing internal audit effectiveness in many companies, this is seen mainly when the ratio between the number of internal auditors and employees grows; the CAE is affiliated to the professional bodies such as IIA; the company adopts control risk self-assessment techniques; and the audit committee is involved in the activities of the internal auditors.

Valencia 2012, suggested five top tips to be considered when measuring the effectiveness of an IAF as follows:

TIP 1: The IAF should go beyond tracking hours

The first tip is with regard to utilisation. Utilisation is calculated as: “Yearly Audit hours = total annual work hours (including vacation, training, administration, etc.) Indicating the percentage of audit field work hours applied to the total annual hours is more valuable to an organisation’s stakeholders than just reporting the number of audit hours”. The IAF should try to compare the utilisation of auditors against each audit’s percentage of completion, as well as the overall percentage of audits completed.

TIP 2: The IAF should measure quality

The IAF should measure quality by defining the quality that IAFs provide to organisations. This indicator of quality lies in the number of times management has requested the services of internal audits. This is made up of the kinds of special requests the IAF receives from management. These could “include fraud investigation, project management, IT advice, policy procedures, or process

improvement efforts. This starts by defining how the IAF provides value to the organisation. Once the quality has been defined, the IAF can begin monitoring and measuring its value”.

TIP 3: The IAF should evaluate skills

The IAF should quantify its team’s audit skills by tracking the average number of years of audit experience; the number of annual hours of training per internal auditor; the number of certifications held by each staff member; each member’s duration with the company/ industry; etc.

Some IAFs have rotating programmes where internal auditors, after a certain period of time, move into operations at managerial level. Try tracking the number of staff who have been successful with the rotational programme, those trained in the IAF, and those moved into operations. This way, the IAF can demonstrate how the function produces some of the organisation’s best and brightest talent within management.

TIP 4: The IAF should show them the money

It is obvious that every CFO wants to see recommendations from the IAF for cost savings, expense reduction, and cost containment. However, if the IAF is more compliance-driven and cannot quantify the cost savings per audit, then they should show the number of major compliance findings, and map these findings with the number of recommendations accepted by management. According to the type of recommendation, the IAF could also assign a “value driver” (e-risk management, fraud, process improvement, compliance). An integrated audit infrastructure plays an important role in streamlining the whole audit lifecycle, and consolidating enterprise-wide audit findings into a centralised framework”. This transcends restrictive organisational silos, and improves partnership and team work on complex audit processes. Another way to measure productivity in terms of cost is to track the number of internal auditors against the recommended number of employees per industry standard.

TIP 5: It all comes down to the finish

In the end, the audit report is proof of the work performed by the IAF, and is the most visible document of the audit engagement. So the question is how informed are those for whom this report is intended?

Before the internal auditor issues an internal audit report, he/she should look at the number of meetings that they have attended with the clients and stakeholders, and examine the content of the meetings. The internal auditors should establish if the client has understood the objectives of the audit, its scope, and of course, its findings, and make sure that those findings are validated by the client. Otherwise, the IAF could end up with mistakes in data, causing loss of reliability.

Internal auditors must ensure that the audit report includes a list of the recommendations implemented, and determine whether the audit report will “hit the stakeholders between the eyes”, and if management will immediately realise the point of the report. A good rule of thumb is to ensure that at the beginning of the report, the following is addressed:

- The importance of the audit (i.e. why does this audit matter?)
- The creation of a sense of urgency (i.e. the desire to address the audit findings)

By applying these tips, one should be able to quantifiably measure the value-added by the IAF.

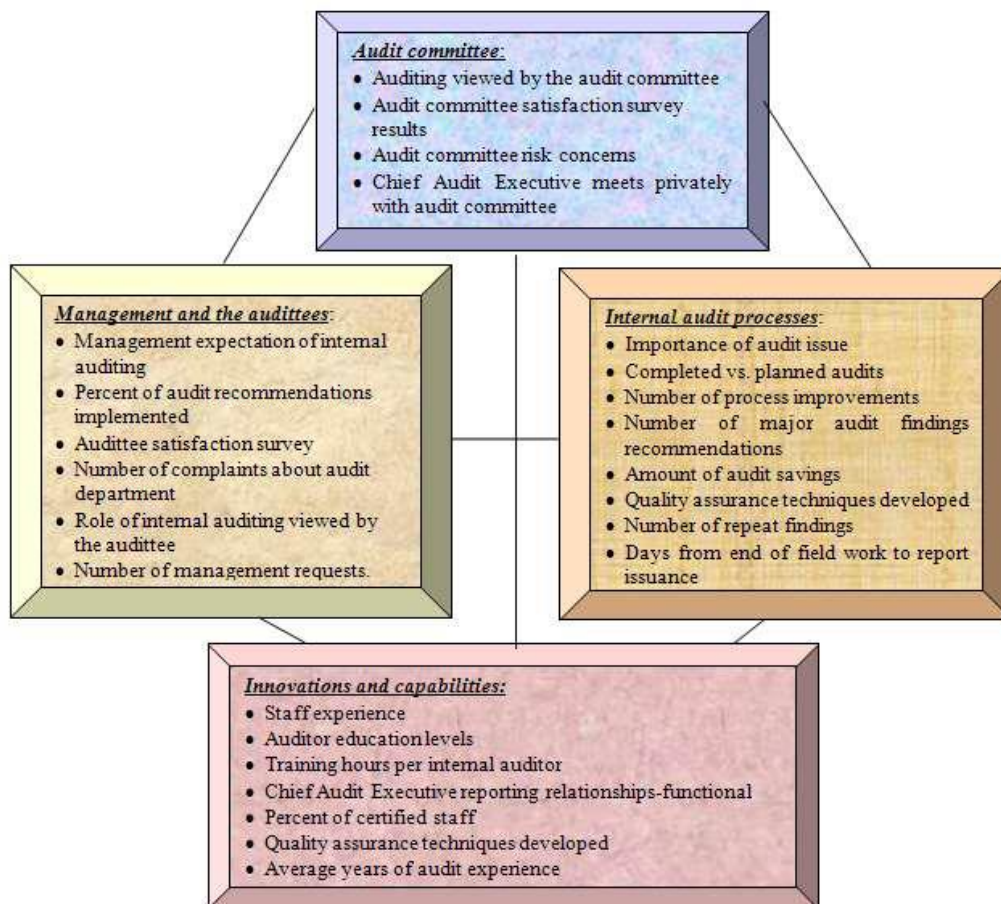
4.7.1 Balanced scorecard

The Balanced Scorecard developed by Kaplan and Norton (1996: 25) is seen as an instrument whereby financial controls and non-financial controls can be measured. It enables an effective monitoring and control tool for an IAF.

Frigo (2002) researched and introduced the Balanced Scorecard (BSC) as an instrument for evaluating the effectiveness of an IAF. According to Frigo (2002), the balanced scorecard instrument emphasises the different ways that IAFs can improve their activities regarding the measuring of the IAF’s performances across the board. The balanced scorecard framework presented by Frigo is approached with a few key elements and views such as: internal audit customers (audit committee, management, and the auditees); internal audit process; and innovations and capabilities. For the creation of this framework, Frigo starts from the idea that some key concepts of this framework could be applied for the IAF: measuring the performance from the customer’s view point; determination of certain indicators for quantifying the internal audit performance; the connection between internal audit and customer expectation; focusing on general strategies of the department and the innovations and capabilities of internal auditing.

Kaplan and Norton (1996) stated that the use of the BSC has become prevalent as a performance measurement and management system in businesses today. The fundamental principle of this approach is based on the notion that assessment of a business should not be limited to a traditional financial evaluation, but should be complemented with measures concerning customer satisfaction, internal processes, and learning and growth. Kaplan and Norton further proposed a three-layer structure for each of the four perspectives, namely: mission, objectives, measures from which targets are to be established, and initiatives to be launched to reach a better rate. To leverage the scorecard as a management instrument, it should be improved with cause-and-effect relationships among measures.

Figure 4.3: Balanced Scorecard framework for IAF



Source: Frigo (2002)

In conclusion, based on the discussion on the balanced scorecard, from the turbulent economy experienced recently it is clear that IAFs are facing challenging tests, one of them being proving their significance and need within organisations. In this context, the added value delivered by the IAF becomes increasingly important. The IAFs need to be more interested in finding the most appropriate methods for measuring and assessment of IAFs effectiveness and efficiency. There are many methods and tools that could combine qualitative with quantitative elements to achieve this, such as those shown in Figure 4.2 in which all the important stakeholders in the IAF and what should each stakeholder measure from the BSC.

The above discussion based on different studies conducted mainly by the big four audit firms, indicated that various methods are used to measure the performance of an IAF, such as the BSC. This section specifically focused on the methods relevant to measuring the performance of IAFs within municipalities in South Africa, as opposed to the methods used in other sectors.

4.8 TRAINING OF INTERNAL AUDITORS

According to standard 1210, the IAF should collectively possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities (Standards, 1210). This can be interpreted by saying that knowledge, skills, and other competencies are a collective term that refers to the professional expertise required of internal auditors to effectively perform their professional responsibilities. Internal auditors are encouraged to prove their expertise by obtaining appropriate professional certifications and qualifications, such as the Certified Internal Auditor designation, and other designations offered by The Institute of Internal Auditors and other appropriate professional organisations.

The MFMA Act of 2013, requires each municipality to have an IAF. This Act provides that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and for this purpose should take all reasonable steps to ensure that the municipality has and maintains effective, efficient, and transparent systems of internal audit operating in accordance with any set standards and norms.

Internal auditors today practice one of the world's most challenging professions. In the international corporate world there have been several company failures resulting in a renewed focus on governance and the accountability of executive management and directors. In the public sector, governments are under pressure to deliver services, secure foreign investment, maintain economic growth, reduce international money laundering and to apply good governance, all of which add to the challenges to both internal auditors and the IAFs.

Expectations of internal auditors within municipalities in South Africa are even more challenging due to South Africa's leading position on the African continent. The fact that this country is considered by the rest of the world to be a success story in its change to a democratic government, and a leader in the inculcation of good governance practices, adds to this challenge. Recently, the World Bank sponsored a conference in Kenya, in collaboration with the Institute of Internal Auditors Incorporated (IIA Inc.), and supported by the Institute of Internal Auditors South Africa (IIA SA). The objective was to promote the profession and concept of internal auditing in Africa. This conference was attended by senior government officials and internal auditors from Kenya, Uganda, Ethiopia, and Malawi.

According to Nel (2015), IAFs and internal auditors are currently facing the following challenges in their work.

4.8.1 Legislative changes

The introduction of the Local Government: Municipal Finance Management Act (MFMA) (Act 56 of 2003), has required the introduction of an IAF in all municipalities and state entities. The most positive impact of IAF in South African municipalities is that internal audit has become a key tool in the governance structure of government, from local authorities through to the parliamentary level. Reliance can now be placed on information carried forward to management by audit committees, especially in respect of the operational efficiency of institutions. The rapid expansion of the public service has presented greater opportunities for advancement, especially for heads of departments, and this has resulted in a shortage of mature and experienced internal auditing staff. This gap can be addressed by training, co-sourcing and learnerships to support the newly established IAFs.

Co-sourcing is the contracting of specialist internal audit practitioners for a period of time to provide internal audit services under the guidance and leadership of the institution's internal audit activity, often whilst transferring knowledge and skills by on-the-job training. A learnership is a work-based learning programme which usually consists of two elements – an educational (academic) component, and a training (workplace instruction) component. It relates to an occupation, and upon completion, leads to the awarding of an academic qualification and/or a professional designation.

South Africa has two registered internal audit designations, namely the (entry level) Internal Audit Technician (IAT, SA) and the (intermediate level) Professional Internal Auditor (PIA, SA). The (advanced level) Certified Internal Auditor (CIA) is an internationally administered and recognised designation that is awarded after candidates fulfil specified academic and work experience requirements, and successfully complete a four-part examination.

Two IAT learnerships have been registered with the Department of Labour and have a total of 65 learners in the programme. The development of the General Internal Auditor (GIA) is currently underway. The IAT qualification (designation) awarded on satisfactory completion of the learnership, is registered on the National Qualifications Framework at Level 6.

4.8.2 Audit committees

The formation of audit committees in the government sector bodes well for the advancement of good governance in government. Transparency of reporting has contributed to world markets' positive view of South Africa. However, the responsibility attached to the accuracy of reporting is

increasing, and applying added pressure on audit functions to perform their tasks to the highest standards.

The recent formation of audit committees carries several opportunities and challenges for internal auditors. Executive management defers to audit committees for expert opinion and guidance, particularly in finance and risk management, and audit committees in turn expect expert comment and support from internal auditors. Audit committees, as a key part of the direct reporting line, therefore have the potential to "make or break" an IAF. The quality of audit committee members is critical, to both the organisation and to the IAF. In the private sector, committee members are required to be board members, where expertise can be attracted more easily as the private sector does not have the financial constraints applicable to the public sector.

4.8.3 Standards changes

The international internal audit standards have been changing over the recent years. The most significant change in international internal audit standards is probably the requirement for an external quality assessment of an IAF which came into effect from the 1 January 2017. The objective of this requirement is to ensure that internal audit activities meet a minimum standard throughout the world, and is intended to significantly strengthen the reliance placed on the work of the internal auditor. In the process, internal auditing will achieve international recognition as an effectively self-regulated profession.

Only if the IAF is issued with an assessment statement that it "Generally Conforms" to the Standards of the IIA, the term "conducted in accordance with the International Standards for the Professional Practice of Internal Auditing" may be affixed. Any serious deviances from the International Standards must be reported as such, and the IAF will then be required to correct the inconsistency and be re-evaluated thereafter to attain the "Generally Conforms" status.

According to Attribute Standard 1300 the IAF is also required to implement an internal quality assurance and improvement program to ensure that there is ongoing review and monitoring of the performance of the IAF". The Attribute Standard 1300 further requires that "each part of the program should be designed to help the IAF add value and improve the organisation's operations and to provide assurance that the IAF is in compliance with the Standards and Code of Ethics of the Institute of Internal Auditors.

The IIASA has developed a high-level initial self-assessment tool, available to members, to assist CAEs and Heads of Departments to do quick assessments to determine the major weaknesses in their processes when measured against the standards. This tool does not provide a full self-assessment, as this is often a complex and time-consuming exercise, but it is nevertheless well worthwhile. In addition, the IIA SA offers a Quality Assessment service which is performed by highly qualified individual team leaders supported by volunteer team members.

Although the MFMA has been implemented for some time now, it is still challenging for these growing IAFs to adhere to these standards. This is especially the case in municipalities, where section 165 of the MFMA requires municipalities to have an IAF. As this is a function many municipalities do not have, to start up this audit function and have it ready for assessment the IIA in 2017 required dedicated effort on the part of the CAEs. They need to expend large amounts of effort to ensure that the correct internal audit quality assessment processes are set up during start-ups, often with limited and frequently over-extended resources, without compromising the delivery of high quality audits.

4.8.4 Enterprise Risk Management (ERM)

Enterprise Risk Management (ERM) is defined in the draft publication of the Committee of Sponsoring Organisations (COSO) ERM framework, as follows:

“Enterprise risk management is a process effected by an entity’s board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risks to be within its risk appetite, to provide reasonable assurance regarding the achievement of the entity”.

It is clear that the internal auditors need to understand the risks facing their municipalities. These risks are not limited only to financial, but operational as well. It is in the efficiency and effectiveness of the operations that real value is created for the clients of state institutions. Internal auditors also need to understand their role in the risk management process. They are not required to set up the risk profile of the institution, but rather, they are required to:

- Perform a monitoring role over the management of the risks and the related control mechanisms;
- Evaluate the risk management process itself; and

- Provide feedback to the risk management function and to management on risks identified during the audit process that are not present in the risk profile of the organisation, particularly where there are significant differences between the evaluation of the severity of the identified risks by management and by the internal audit.

The IAFs need to be recognised and supported by audit committees, executive management, and executive authorities. There are a number of essential characteristics that lead to this recognition, as suggested by Lesejane (2004):

Code of ethics – internal auditors must be seen to uphold the code of ethics of the IIA and the ethical integrity of the organisation. Internal auditors are regarded as the icons of organisational ethics.

Visibility is achieved by using all the methods of communication, verbal, written and graphical, to enhance the delivery of higher than expected quality audit quality work.

Objectivity – sticking to an objective point of view by avoiding trying to score points.

Innovation is the continual re-invention of internal audit activities in a changing environment. It ensures focus on value-adding activities, and is key to the performance of an internal auditor's work. Furthermore, internal auditors need to be aware of changes in their environment and new organisational requirements, and act upon those changes timeously. They must prove, with facts, the wisdom of decision-making through deductive reasoning, as this may turn managements' and the business decision-making in the right direction. It is mandatory for internal auditors to create an effective information network – not an information technology network – but one that feeds information to the IAF. Finally, internal auditors must understand management's organisational style, and adapt the auditing approach to suit that style without compromising the quality of internal audit work.

The Challenges facing internal auditors are undoubtedly limitless, as new laws and regulations, and changing world conditions differently affect each organisation for which internal auditors work. It is only the individual internal auditor who can make a difference in improving the status and effectiveness of the profession. This requires delivery of internal audit services that add value to the organisation. Auditing is not a profession for the cowards. It is for those who are bold enough to demonstrate their objectivity and independence, and influence all to perform in the best interests of the stakeholders of the entities that employ them (IIA, 2009).

4.9 AUDITING MUNICIPALITIES IN SOUTH AFRICA

According to De Bruin, Du Plessis and Grobler (2001: 13), “the need for the establishment of an IAF was first started in the public sector in South Africa with the promulgation of the Reporting by Public Entities Act of 1992 (Act 93 of 1992). This Act required all public entities to establish an IAF”. This requirement for having and establishing of an IAF was extended to all national and provincial government departments in 2000, with the implementation of the Public Finance Management Act (Act 1 of 1999) and Municipal Finance Management Act (Act 56 of 2003).

4.9.1 Establishment of IAF in a municipality

Section 165 of the MFMA prescribes the establishment of an IAF within a municipality. This function is considered to be an important component of internal control, risk management and corporate governance, and provides the necessary assurance and advisory services to the municipality. IAF is one of the most significant management tools available to municipal authorities, and can provide value-adding services to the municipality or municipal entity when objectively and adequately resourced. The MFMA requires that municipalities should afford the IAF the space to be in a position to provide management with assurance regarding the effectiveness of the system of internal controls, risk management and governance processes.

Section 62 of the MFMA further requires that the Accounting Officers (AO) of municipalities take all reasonable steps to ensure that the municipalities have and maintain effective, efficient, and transparent systems of internal audit, and that they operate in accordance with any prescribed norms and standards. This can be ensured by the establishment of IAFs.

4.9.2 Independence and objectivity within the IAF of a municipality

The MFMA requires the CAE of the municipality to report at a level within the municipality or municipal entity that allows the IAF to fulfil its responsibilities. Such a level must have enough authority to promote independence and to ensure broad coverage, adequate consideration of engagement communication and appropriate action on engagement recommendations. The CAE is required to report functionally to the audit committee, and administratively to the AO. Independence is achieved through the organisational status and the objectivity of the IAF. Direct communication between the CAE and senior management takes place when the CAE regularly attends and participates in meetings relating to its oversight responsibilities for auditing, financial reporting, corporate governance, and control. The presence and participation of the CAE at these

meetings provides an opportunity to exchange information concerning the plans and activities of the IAF.

It is required that each internal auditor within a municipality should have an objective attitude and should be in a sufficiently independent position to exercise judgment, express opinions, and present recommendations with neutrality. An internal auditor within a municipality should be free of any conflict of interest arising from professional or personal relationships or other interests, and should not be subjected to any undue influence that restricts or modifies the scope or conduct of the audit work, or the content of any internal audit report.

Therefore, the IAFs within the organisations including the municipalities are required and expected to have no direct working responsibility or authority over any of the activities being reviewed, nor develop or install systems or procedures, prepare records, or engage in any other activity that would normally be audited. The IAF must not initiate or approve accounting transactions external to the scope, and avoid conflict of interest. In conclusion, to remain trusted and effective, the IAFs need to be independent within their municipalities they serve.

4.9.3 Auditing requirements for municipalities in South Africa

According to the MFMA, the chairpersons of the audit committees of all municipalities are required to report to the municipal council on the operations of the IAF and the audit committee on a quarterly basis, or even more often if required. The audit committee's audit report should include:

- A summary of work performed by the internal audit and the audit committee against the annual work plan;
- Effectiveness of internal controls and additional measures that must be implemented to address identified risks;
- A summary of key issues dealt with, such as significant internal and external audit findings, recommendations, and the updated status thereof;
- Progress with any investigations and their outcomes;
- Details of meetings and the number of meetings attended by each member; and
- Other matters requested of the internal audit and audit committee.

The audit committees of all the municipalities are therefore required to prepare an annual report to be included in the municipality's annual report and those of its entities. Such an annual report should include the following, among others:

- Description of the functions performed by the municipality's audit committee and meetings attended in the financial year;
- Resolutions taken by council and implementation status of recommendations made; and
- Other relevant comments that may enhance governance and accountability within the municipality.

According to the MFMA, the chairperson of the audit committee should submit a copy of the audit committee's report at least yearly, or at other agreed intervals, to the Municipal Public Accounts Committee (MPAC), for consideration during the MPAC engagement with the oversight report. The MFMA further requires the chairperson of the audit committee to be available at all times should MPAC needs clarity on the report of the audit committee. Therefore, the roles and responsibilities and outputs of both the IAF and audit committee help to inform the work of the MPAC and its oversight structures (MFMA).

4.9.4 Responsibilities and roles of IAF within a municipality:

According to the MFMA the IAF of a municipality is accountable to the audit committee in the following ways:

- By maintaining open and effective communication with the audit committee;
- Developing a flexible annual audit plan using a risk-based methodology, addressing any weaknesses in risks or controls identified;
- Submitting the audit plan to the audit committee for review and approval;
- Reporting on the implementation and results of the annual audit plan, including special tasks requested by management and the audit committee;
- Assisting in drafting the agenda and other documentation, and facilitate the distribution thereof to the audit committee in advance of meetings;
- Meeting periodically with the chairperson of the audit committee to discuss whether the material and information furnished meets the requirements of the audit committee;
- Obtaining advice from the audit committee whether the frequency and time allocated to the committee is sufficient to attend effectively to all matters;
- Cooperating with the audit committee as they conduct annual reviews of the performance of the IAF; and
- Submitting the internal audit charter to the audit committee for review and approval on an annual basis and as necessary.

The points listed above indicate the extent to which IAFs need to assist the audit committees to function and perform as expected. It is still to be established by this study whether the IAFs in municipalities assist the audit committees in performance of their tasks as expected by senior management (MFMA).

4.9.5 Challenges faced by municipalities in South Africa

According to the MFMA Circular No. 65 issued by the National Treasury of South Africa, recent audit findings by the AGSA, have highlighted serious deficiencies in governance arrangements within municipalities in South Africa. This presents a dire need to improve the effectiveness of both the IAFs and audit committees, as this would contribute to changes in financial management in the vast majority of municipalities (National Treasury).

According to the AGSA 2012/13 municipal audit report, the operations of 28% of the IAFs did not fully comply with the legislated requirements. The most common non-compliance findings were found to be inadequate assessment of, or reporting on, internal controls, accounting, risk and loss control, and insufficient auditing of the results of performance measurements or not auditing them on a continuous basis as expected. It was further found that all the IAFs did not report to the audit committees as required by legislation. All these identified weaknesses within municipalities are considered to be major weaknesses, as the IAF exists to assist those in authority/senior management with the key areas mentioned in the AGSA report. This raises the question of whether the IAF within municipalities are effective or not. If they are unable to perform key duties within their sphere, they must be regarded as ineffective and not adding value.

According to the MFMA Circular No.65, the AGSA has mentioned that these deficiencies within municipalities result from lack of knowledge or a disregard of legislative processes by councillors and officials; failure to appoint suitably qualified key individuals to specifically legislated tasks; and an inability or disregard by municipalities to establish and maintain the appropriate control systems which support the governance framework. The AGSA 2013 report (AGSA, 2013, 35) stated that only 17 out of 278 municipalities audited by them obtained unqualified audit reports. Six out of eight category A municipalities failed their audits. Together they accounted for over R170 billion of the municipal budget (Seale, 2013: 1). As part of governance structures, IAFs must ensure that they report on critical issues to assist municipalities achieve their financial objectives and their delivery issues, which contribute to municipalities obtaining qualified audits (AGSA, 2011:32; Auditor-General South Africa, 2012: 86; Auditor-General South Africa, 2013: 31, 35, 75, 103). The Auditor-General South Africa stressed the fact that audit committees must be strengthened (Seale, 2013: 3).

The following studies support the challenges mentioned above that still face South African municipalities. A report issued by SALGA in 2007 identified important issues regarding the capacity of councillors to run their municipal areas. The report indicated that there “was insufficient legal support and advice available to councils, which led to serious decision-making mistakes. In some cases, the roles of councillors were not clearly defined, and 60% of those who participated in the survey were first-time councillors. Kanyane (2006: 116) highlighted the weak leadership in strategic management, including corporate governance; shortage of skills to implement financial management; legislation; misplacement of skills within municipalities; and political considerations in appointment of senior managers without the required qualifications, had tremendously weakened the performance of municipalities in general.

Some municipalities were found to have inadequate financial management capacity, which resulted in weak budgetary functions, accounting, credit control, and financial reporting systems. The 2008/09 AGSA audit report revealed that about 60% of the 283 municipalities could not at that stage provide evidence to account for the revenues they had received (AGSA, 2008). Thus, municipal managers and financial officers were unable to show how and when financial allocations from government had taken place, and were unable to provide proof of where the amounts listed in their financial statements originated from (AGSA, 2008).

In June 2009, the Department of National Treasury reported to the Technical Committee for Finance that 56 local municipalities and eight district municipalities were on their financial distress list. Most of these local municipalities were identified as being in the Eastern Cape Province, the Free State Province, and the Northern Cape Province. The remaining were in other provinces of South Africa (Koma, 2010).

In conclusion, it is therefore evident that there are some shortcomings within municipalities in South Africa, as highlighted by the AGSA reports, the National Treasury and the other studies indicated above, which persuaded the researcher to undertake this study with the aim of investigating what the IAFs within the municipalities were doing when all these weaknesses manifested. IAFs are expected to assist municipalities in dealing with identified deficiencies, and to develop a conceptual framework that can be used to assist IAFs within local government to become effective and add the required value.

Summary

The section above discussed how municipalities in South Africa should be audited, according to the legislation that guides this. The role of the AGSA as the main player available for ensuring that municipalities are audited and comply with the requirements regarding finances were fully discussed in the section. This discussion included the challenges identified by previous audits of municipalities in South Africa, such as lack of capacity and poor decision-making.

The following section looks at how the National Treasury views the effectiveness of IAFs in South Africa, and focuses on two of the key elements investigated in this study, namely, value-adding and effectiveness.

4.10 VIEWS ON EFFECTIVENESS OF IAF IN THE PUBLIC SECTOR IN SOUTH AFRICA

A study conducted by the Department of Treasury in South Africa in 2014, revealed the following findings regarding the status and demand for IAFs in national departments (Treasury, 2014):

4.10.1 With regard to independence of internal auditing:

The study participants indicated that the reporting lines within their national departments comply with the recommendations of governance codes and to the Institute of Internal Auditors (IIA) guidelines. Internal auditing in South African national departments can thus be regarded as sufficiently independent organisationally. However, the gaps in the perceptions of AOs, Chairpersons of Audit Committees (CACs), and Chief CAEs regarding the reporting structure in some of the departments, is a matter of concern, as it is assumed that these parties would be aware of the reporting lines of their IAF. This means that the main stakeholders within these departments are more concerned with the reporting lines that the IAFs are taking. This is something, among others, that the study tried to establish while researching the municipalities.

4.10.2 With regard to value adding:

The study found that the outsourced IAFs seemed to be adding more value within the national departments than in-house IAFs. This could be attributed to the lack of appropriate training and experience undermining the capabilities of in-house IAFs. This was also being investigated by the researcher in an attempt to find out why the key stakeholders believed in outsourced IAFs rather than in-house IAFs.

4.10.3 With regard to prevention and detection of fraud:

The participants indicated that the in-house IAFs were, to a large extent, still regarded as being required to fulfil a “watch dog” function in respect of fraud prevention and detection, while the internal audit profession in general regards this as the responsibility of management.

4.10.4 With regard to competencies of IAF staff:

The study found that the skills and competencies profile of CAEs in national departments was lower than the profile recommended by the IIA, as documented in its formal career path guidelines. The IIA recommends that CAEs should be qualified as Certified Internal Auditors (CIAs) as well as being in possession of academic master’s degrees.

The study found that staffing of IAFs was insufficient in number and quality to empower IAFs to provide the level of service expected by their stakeholders. This research identified that “this could

be attributed to the fact that CAEs are not adequately qualified (academically or professionally); that too many vacancies exist; that staff turnover rates are too high; and that the level of internal audit experience (the number of years of first-hand experience) is too low for the demands of the job. The study therefore recommends that careful steps be taken to ensure open communication between AOs, CACs and CAEs". It is further recommended that national departments build in-house IAFs capacity, improve their status within national departments, and ensure that they will be able to meet the expanding expectations of their stakeholders. The expectations of the stakeholders are very important, as these become the clients of the IAFs in the public sector.

Summary

The discussion above outlined results from the study conducted by the Department of National Treasury on IAFs within national departments, and identified the key findings of the study. It was clear that the key stakeholders in the study, being CAEs, CACs and AOs, and highlighted major concerns to be addressed in order to have a fully-fledged IAF that is effective. The concerns that raised in the study, assisted the researcher in formulating relevant questions to the major stakeholders within the municipalities.

4.11 INTERNAL AUDITING AND ITS ROLE

The IIA (2016: 2) defines internal auditing as "an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations, which assists organisations in achieving their goals by employing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes". Goodwin (2012: 642) argues that this definition suggests that the role of internal auditing within the organisations has continued to change from financial and compliance audits to a wider value-adding role, embracing both assurance and consulting activities and focusing on improving performance and effectiveness.

The Institute of Internal Auditors (IIA) definition of internal auditing refers "both to the assurance and consulting activities directed at governance, risk management, and internal control processes". Consequently, an IAF that fulfils this definition is the one that is distinctively positioned to support the organisation's management as an essential component of their governance mechanisms (ECIIA, 2005). Moreover, "Carcello, Hermanson and Raghunandan (2005) found indications that, due to the enhanced focus on corporate governance, effective oversight, and sound internal controls, the importance assigned to IAF by management has increased. Furthermore, they suggest that senior management's expectations of the IAF have changed in many ways".

The IIA (2012: 10) further describes an IAF as “an important internal assurance instrument available in public financial controls, and as a tool that can be used for monitoring and evaluating managerial activities before an audit is conducted by external auditors. Internal auditors are viewed as professionals who can boost honesty and fairness, decrease dishonesty, and ensure value for money in public spending”. An IAF is seen as an important element of any public-disbursement-related management system, and should ensure that public spending is within controlled budgetary provisions. Additionally, procurements must comply with specified procedures, as well as provide for the timely reconciliation of accounts, effective systems for management, and the accounting of physical and financial assets. IAFs are expected to work with management within their organisations to improve service delivery and ensure compliance with applicable laws, provide independent and objective assurance to an organisation’s management that its risks are being mitigated to an acceptable level, and report when they are not.

Senior management and the board may desire objective assurance and advice on risks and controls. An adequately-resourced IAF can provide such assurance and advice (UK Turnbull Guidance, 2005). A professional IAF supplements senior management’s actions by providing independent and objective assurance on the effectiveness of the organisation’s governance processes, how well it manages all kinds of risks, and whether internal control processes are operating, as required, to manage risks to an acceptable level. In other words, management receives an independent and objective assurance on the quality of internal controls from someone other than the management or line managers receives independent and objective assurance on the quality of internal controls from someone other than the line managers and decentralised finance staff. Furthermore, the IAF can play a key role in monitoring the organisation’s risk profile and identifying areas in which to improve risk management processes. The IAFs also support management by providing consulting services, which contribute to the establishment of sound risk management processes, by facilitating management’s efforts to improve the system of internal controls, and by giving advice on the implications of organisational changes to the system (ECIIA, 2005; Leithhead, 2000; Lindow & Race, 2002; Page & Spira, 2004; Spira & Page, 2003).

Besides the valuable supportive role that the IAF can play for senior management, a solid and constructive relationship with senior management is also critical for effective functioning of the IAF (ECIIA, 2005). More specifically, Standard 1110 of the International Standards for the Professional Practice of Internal Auditing (Standards) stipulates that the CAE should report to a level within the organisation that allows the IAF to accomplish its responsibilities. On the other hand the related Practice Advisory 1110-2 recommends that, “besides having a functional reporting relationship with

the audit committee, the CAE must have an administrative reporting relationship with senior management (preferably, the senior manager or another executive with sufficient authority), in order to achieve the appropriate support to achieve internal audit's day-to-day activities. In general, this support should include positioning the IAF and the CAE in the organisation's structure in such a manner that affords appropriate stature to the function within the organisation (e.g. unrestricted access to staff, information and documentation) (standard 1110).

According to Dittenhofer (2001), when evaluating the effectiveness of the internal auditing operation, a positive response would be given when the internal auditor: audits the achievement of the auditees' objectives and finds no problems, and no problems surface following the audit; or audits and finds problems, and recommends solutions to the problems, and the solutions resolve the problems. From this statement it is clear that outcomes address a wide range of aspects i.e. all the elements on which audit activities have an impact. These include both efficiency and effectiveness of the audited processes, and corporate performance. At a process level, for example, the impact of internal audit activities can be related to cost savings generated by the implementation of suggested recommendations (Cashell & Aldhizer III, 2002).

Sarens (2009), based on Gramling et al. (2004), suggested that IAFs can be considered effective when the quality of the IAF "has a positive impact on the quality of corporate governance. Sarens (2009) also linked IAF quality to the capacity to monitor and improve risk management and internal control processes.

The effect that internal auditors have on the achievement of organisational objectives (i.e. their effectiveness) is influenced by the extent to which organisational managers consider internal auditors' work valuable and decide to exploit it. In such a view, the effectiveness of IAF depends on its quality perceived by the auditees, given the central role of auditees' perceptions in relation to IAF effectiveness.

4.12 REPORTING BY IAFS

The IAFs perform their functions within their organisations, which include municipalities, and report their activities in a written report called an audit report. According to Ackermann (2014: 116), the audit report is "an important output as it provides users such as audit committees and management with information on matters affecting their decisions".

On the other hand the Standard 2400 states that internal auditors must communicate the results of their engagements to their organisations. This communication must include the engagement's

objectives and scope as well as applicable conclusions, recommendations, and action plans (standard, 2410). This standard also emphasises important criteria and points to be included in the communication of the IAF results to the organisations. This means that the internal audit reports must, where appropriate, contain the internal auditors' opinion and/or conclusions. When issued, an opinion or conclusion must take account of the expectations of senior management, the board, and other stakeholders, and must be supported by sufficient, reliable, relevant, and useful information (standards). Opinions at the engagement level may be ratings, conclusions, or other descriptions of the results". Such engagements may be in relation to controls around a specific process, risk, or business unit. The preparation of such opinions requires consideration of the engagement results and their significance.

Standard 2420 continues to explain that the communication of audit results through the audit report must be accurate, objective, clear, concise, constructive, complete, and timely. (Standards, 2420). The standard further explains each characteristic of an audit report. Accurate communications mean results that are free from errors and distortions and are faithful to the underlying facts. Objective communications are those that are fair, impartial, and unbiased, and are the result of a fair-minded and balanced assessment of all relevant facts and circumstances. Clear communications mean those results that are easily understood and logical, avoid unnecessary technical language, and provide all significant and relevant information. Concise communications are those that are to the point and avoid unnecessary elaboration, superfluous detail, redundancy, and wordiness. Constructive communication is helpful to the engagement client and the organization, and lead to improvements where needed. Complete communications lack nothing that is essential to the target audience and include all significant and relevant information and observations to support recommendations and conclusions. Timely communications are opportune and expedient, depending on the significance of the issue, allowing management to take appropriate corrective action. It is therefore expected that all the internal audit reports provided by the IAFs should adhere to the guidelines and characteristics discussed above. If such characteristics are met by the internal audit reports, they will be considered relevant and value-adding (Standards, 2420).

4.12.1 Errors and omissions in internal audit reports

Standard 2410, indicates that if the final communication or audit report communicated to the users contains a significant error or omission, the CAEs of the IAFs must communicate corrected information to all parties who received the original communication.

4.12.2 Disseminating internal audit results

Standard 2440, states that the CAEs of the IAFs “must communicate results to the appropriate parties (Standard, 2440). This standard emphasises that the internal audit results should be communicated only to the relevant parties. The CAE within the IAF is responsible for reviewing and approving the final internal audit report before being issued, and for deciding to whom and how it will be disseminated. When the CAE delegates these duties, he or she retains overall responsibility. Therefore, the CAEs of the IAFs should consider the following before issuing internal audit results: Communicating the final results to parties who can ensure that the results are given due consideration (Standard 2440).

If not otherwise mandated by legal, statutory, or regulatory requirements, prior to releasing the results to parties outside the organisation, the CAE must:

- Evaluate the possible risk to the organisation;
- Check with senior management and/or legal counsel as appropriate; and
- Control the report distribution by limiting the use of the results.

Standard 2450 further suggests that when an overall opinion is issued, it must consider the expectations of senior management, the board, and other stakeholders, and must be supported by sufficient, reliable, relevant, and useful information.

The communication of results will “identify the scope, including the time period to which the opinion pertains; the scope limitations; consideration of all related projects, including the reliance on other assurance providers; the risk or control framework, or other criteria used as a basis for the overall opinion; and the overall opinion, judgment, or conclusion reached. Reasons for an unfavourable overall opinion must be stated” (Standard, 2450).

4.12.3 Monitoring progress made on internal audit reports

Standard 2500 states that the CAEs must establish and maintain a system to monitor the nature of results communicated to management and other relevant parties. The CAEs must 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. The IAFs must therefore monitor the nature of the results of consulting engagements to the extent agreed upon with the client.

4.12.4 Communication of acceptance of risks

When the CAE concludes that management has accepted a level of risk that may be unacceptable to the organisation, “the CAE must discuss the matter with senior management. If the CAE determines that the matter has not been resolved, he/she must communicate the matter to the board” (Standard, 2600). The identification of risk accepted by management may be observed through an assurance or consulting engagement, monitoring progress on actions taken by management as a result of prior engagements, or by other means. It is not the responsibility of the CAE to resolve the risk.

4.13 COMMUNICATION OF INTERNAL AUDIT RESULTS IN SOUTH AFRICAN MUNICIPALITIES

In South Africa, a section under internal audit – Section 165(b) (i–iv) of the MFMA, indicates that the IAF is required to “advise the AO and report to the AC on the implementation of the internal audit plan and matters relating to internal audits; internal controls; accounting procedures and practices; risk and risk management; and performance management. It is expected that all the internal audits, will be continually conducted in municipalities by their internal auditors through IAFs, as required by the MFMA” (MFMA, 2003).

The annual financial statements are the most important record of the financial status of municipalities and municipal entities. Every municipality and municipal entity in South Africa must prepare annual financial statements for each financial year, and submit it to the AGSA for auditing no later than 31 August of each year. In the case of a municipality with municipal entities, the municipality is also required to submit consolidated annual financial statements to the AGSA no later than 30 September of each year.

The MFMA requires that every municipality and municipal entity “must prepare an annual report for each financial year. The annual report is a key instrument of transparent governance and accountability, and must be used to measure performance for the year. The early completion and submission of annual reports, together with the annual financial statements, facilitates timely and

improved information for the oversight bodies". The oversight of annual reports represents the final stage in the accountability cycle. Once approved by the council, the annual report must be placed on the municipal website, made available to the wider community, and copies must be sent to various authorities.

In terms of the MFMA, the municipality and each of its municipal entities must have an IAF and an AC which must prepare a risk-based audit plan and internal audit programme for each financial year.

Therefore, irrespective of the type of the municipality, internal audits within the municipalities are conducted throughout the year by the IAFs, and take many forms, such as financial audits, compliance audits, performance audits, and IT audits. The audit findings and audit reports are then submitted to senior management of such municipalities, which ensures that the recommendations made were taken into account while attempting to achieve the municipal objectives, (MFMA).

Once the internal audits have been conducted as indicated above, in order to fulfil the requirement of the MFMA, external audits are normally conducted by the Office of the Auditor-General. Section 92 of the MFMA states that the AGSA is required to audit and express its opinion on the accounts, financial statements, and financial management of each municipal entity. Findings and reports are submitted to the relevant provincial legislature, as per section 21(1) of the Public Audit Act (hereafter, PAA) No.25 of 2004, and section 126 (4) of the MFMA, which states that the AGSA may submit the financial statements and audit report (a) of a municipality directly to the relevant municipal council, the National Treasury, the relevant provincial treasury, the MEC responsible for local government in the province and any prescribed organ of state, if the mayor fails to comply with subsection (2) or (3).

4.13.1 Challenges experienced by IAFs within municipalities

According to SALGA, from an operational perspective, there is a general lack of technical skills and the necessary knowledge for performing key duties in financial management. This is a major constraint, and one of the biggest challenges that face municipalities. These technical skills include planning, engineering, project management and plant operation. Inadequate capacity at the senior management level, and a lack of appropriate financial management skills in municipalities results in poor service delivery. Furthermore, a high turnover of senior management is a major issue affecting the ability of municipalities to expand and improve service delivery. The financial management support programme for municipalities has provided support for local government

financial management reforms since 2003. These were targeted at the larger municipalities with greater capacity to implement the reforms as they were phased in. The programme operates through the provision of grants and technical advisors to municipalities to assist in implementing the MFMA. A quarterly MFMA coordination committee representing national and provincial departments and SALGA, was established in 2004, to receive updates on progress in implementing the financial reforms and to assist in addressing challenges in a coherent and sustainable way.

4.14 THE FUTURE OF INTERNAL AUDITING

4.14.1 Future of IAFs

According to Crowe Horwath (2015, <http://www.crowehorwath.com/ContentDetails.aspx?id=10747>) for the IAFs “to be seen as a relevant and valuable contributor to their organisations, the IAFs must shift their focus from traditional regulatory and compliance matters to helping their organisations to manage risk and operations. In doing so, the IAFs need to overcome challenges related to governance, staffing, operations, and quality, as well as focusing on the big picture. This type of change is transformational, and it requires IAFs to take a bold new look at its roles and responsibilities, break down old frameworks, and create a new framework for the future”. The time to start this is now.

According to Ernst and Young (2012:22), the IAFs may have charters and annual plans, but many do not have a higher-level, internal audit-specific strategic plan. A detailed strategy enables IAFs to align their objectives to the organisation. The IAFs strategy should have a long-term (e.g., three to five-year) time horizon, and a road map that is based on the organisation’s overall strategy, its stakeholder expectations, regulatory requirements, and the role of the risk functions. Therefore, leading IAFs follow four steps to create a well aligned strategy:

- Develop or refine the IAFs strategic vision. Know the function’s roles, responsibilities, and the needs of its key stakeholders, its mandate, and what the IAF should accomplish over a long-term period.
- Identify and prioritise key strategic initiatives. Based on the mandate and strategic vision, align initiatives to key business risks and key operational and financial priorities. Make sure that processes, methodologies, and tools are up to date, that internal audit has the industry and functional insights it needs, and that staffing frameworks are flexible enough to anticipate change and address emerging risks/issues.

- Design the appropriate key performance indicators (KPIs). Determine how internal audit measures its success against the prioritised initiatives, how it aligns with stakeholder expectations, and how to track productivity and value-driven measures.
- Develop an operating strategy. Detail activities that enable internal audit to achieve its strategic initiatives. Determine key milestones and how the function communicates its progress to key stakeholders. Lastly, put steps in place that enable the internal audit to adapt to changing priorities so that it can maximise its relevance to the business.

It is therefore important for every IAF to have a strategic vision which it can clearly define and understand, to successfully add value to its organisation.

4.14.2 Conducting real-time audit assessments

According to the Ernst & Young (2012), another way to increase the value of the IAF is through real-time audit assessments". Improving the risk assessment process is the number one priority of CAEs and stakeholders alike. Identifying risks that are truly significant to the business is the first step to effective risk management and monitoring. Today's IAFs are focused on enterprise-wide risk coverage, leadership engagement and direct linkage to strategy to increase the relevance of the risk assessment. As well, most leading organisations are incorporating a quantitative component. Data-driven analytics can produce more focused stakeholder discussions, help to frame facilitated workshops, and drive the scope of internal audit reviews. Because risks are always changing in all organisations, an annual risk assessment is no longer enough for internal audit to remain relevant to businesses. Thus, regular risk assessments on enterprise-wide coverage should be the focus, with management participation and a direct link back to the company's overall strategy.

4.14.3 Issue-based audits

Issue-based audits are another way in which the IAFs can add value to their organisations by providing insights on strategic organisational issues. These audits can be ad hoc or planned in advance and aligned to the organisational strategy based on the organisation's request, or unexpected events that occur throughout the year. These audits can include a mix of advisory and assurance reviews. The IAFs would also be wise to build time into the audit plan for potential ad-hoc issues.

Summary

In conclusion, the IAFs can turn risk into results and become more relevant to their organisations by:

- Using the organisation's all-encompassing business strategy to identify the risks that matter most and set the tone for an IAF strategy;
- Developing an internal audit-specific strategy with a three- to five-year time horizon that focuses on stakeholder expectations, coordinates risk functions, and drives internal audit initiatives;
- Employing critical enablers throughout the internal audit life cycle, such as an organisational structure that aligns to the business and fits the organisation's culture, and an appropriate talent management programme that ensures internal audit has the right people with the right skills in the right positions;
- Running the IAF like a business by employing data analytics to drive enterprise efficiencies and results, and by designing a value charter and scorecard that define how value to the organisation is measured and whether IAF is achieving its goals.

With the right internal audit-focused strategy in place, IAFs can add value to their organisations by becoming strategic advisors, identifying efficiencies across the enterprise, supporting key business initiatives, and quantifying internal audit's return on investment. The future of IAFs is not limited, and action needs to be taken now for IAFs to remain relevant to their organisations, or be left behind.

4.15 EVALUATIONS WITHIN THE IAFs

According to Boța-Avram and Palfi (2010) even if the IAFs form an integral part of the of the control framework of an organisation, it is obvious that this function must also have its own controls to track whether its performance is consistent with its role and objectives. The ISPPIA state that: the CAE must develop and maintain a quality assurance and improvement program that covers all aspects of the IAF (1300- Quality Assurance and Improvement Program). According to the interpretation offered by the new version of internal audit standards issued by The Institute of Internal Auditors in 2008 (and applicable in 2009), this program also "assesses the efficiency and effectiveness of the IAF and identifies opportunities for improvement".

In this regard, the challenge of measuring the effectiveness of IAFs is receiving increasingly significant relevance so that IAFs have to find the best and most relevant method for measuring the efficiency and effectiveness of internal audit, and quantify the progress made in achieving its goals and objectives (Boța-Avram & Palfi, 2010).

Value-added delivered by the IAFs is becoming increasingly relevant, which makes it necessary to identify the determinant factors in creating this added value. It is appreciated that in the future, one of the most important criteria for the existence of IAF will be creating value. This will determine the reason for the existence of the internal audit profession. Internal auditing must become a “value creator” while trying to eradicate the unpleasant label of “resources consumer”.

Boța-Avram and Palfi (2010) further suggest the guidelines of measuring and assessment of IAF's effectiveness within organisations from two perspectives, namely, quantitatively and qualitatively. The quantitative method for the measuring internal audits' effectiveness includes the following:

- Determination of fulfilling degree of IAF's plan that consist in establishing the proportion that internal audit activities are realised according to internal audit plan in a certain period of time. This can be measured by determining the number of realised activities reported at a certain planned time period for each type of activity.
- Identification of necessary time period for the issuing of the final internal audit report that consists in determination of the passed time from ending internal audit work to the issuing of final internal audit report, including the plan of actions for the management;
- Monitoring the necessary time for solving internal audit findings. From this point of view, we consider it relevant to realise a statistical data base through which to follow different elements, such as the number of deficiencies solved in the established time, the number of deficiencies solved with delay, and the number of deficiencies unsolved;
- The assessment of personal's certification: from quantitative point of view, that can be determined through the number of staff employees from internal audit department with professional certification diplomas or the professional experience quantified in years of internal audit work;
- Determination of the report between time dedicated to certain internal audit activities and the time dedicated to administrative activities that can be determined through daily monitoring of each internal auditors' time by clearly specifying the types of activities realised during a day's work.

On the other hand, the qualitative method is the most frequently used method for analysing and assessing an internal audit's performance, and includes the following:

- conducting research which could include interviews and/or questionnaires with respondents from the organisation under study; and
- conducting research (interviews and/or questionnaires) with respondents who are the auditees of the organisation under study.

4.16 ROLE OF INTERNAL AUDITING IN THE PUBLIC SECTOR

Public sector managers operate in an increasingly complex and challenging environment. This in part reflects the increasing demands and expectations of the community, the government. And parliament. Public sector managers have a range of resources and mechanisms available to assist them in meeting their responsibilities within this environment.

The IAFs are expected to provide support and activities within the government sector, which enable their sector to fulfil its mandate. These activities include developing the IAF's strategic business plan and internal audit annual work plan; providing support services to the AC; monitoring the implementation of agreed internal and external audit report recommendations and those of legislative committees and other bodies; internal audit staff management and training; and liaison with the external auditor.

The Australian Audit Office (2007) has suggested the following main characteristics for best practice of IAFs in the government sector, which are defined by:

- Operational independence: that is, the IAF is independent from the activities subject to audit.
- Is appropriately positioned in the entity's governance framework to ensure that the work of internal auditors complements the work of other internal and external assurance and review providers.
- Has a well-developed business strategy that clearly articulates the IAF's future roles and responsibilities?
- Is business focused and has audit plans that are comprehensive and balanced, and are linked to the risks in the entity.

- Has the confidence of key stakeholders, including the chief executive, the board (if applicable), the audit committee, and senior management.
- Undertakes all audits in accordance with specified auditing standards.
- Has sufficient financial resources and access to internal audit staff with the necessary skills, experience, and personal attributes to achieve what is expected of internal audit.
- Provides internal audit reports and other services, based on efficient and effective work practices that are valued by stakeholders.
- Provides an annual assessment, based on internal audit work undertaken, of the effectiveness of the entity's system of internal controls.
- Advises the Audit Committee and entity management of patterns, trends or systemic issues arising from internal audit work.
- Facilitates communication between external audit and entity management.
- Distributes lessons learnt arising from work done in relevant areas of the entity.
- Regularly informs the audit committee of progress in the implementation of agreed internal and external audits, and other relevant report recommendations.
- Actively manages any external service providers, and is subject to periodic assessment and review as part of a continuous improvement process.

These characteristics are internationally accepted as the fundamental characteristics that need to be adopted and implemented for the success of IAFs worldwide.

In South Africa, the introduction of the Public Finance Management Act (PFMA) (Act 1 of 1999) in 2000, with its focus on good governance and accountability, made IAFs an essential part of financial management in the public sector. The PFMA requires accounting officers to ensure that their departments have an effective, efficient, and transparent system of financial and risk management, and internal control, and furthermore requires that the National Treasury makes regulations and issues instructions to accounting officers on how to maintain an IAF and to manage its activities. The fundamental purpose of IAFs in the public sector is to assist accounting officers to maintain efficient and effective control in public service institutions by evaluating the controls (specifically, determining their effectiveness and efficiency), and by making recommendations supporting the goal of enhancing and improving governance.

The role of internal auditing within the public sector in South Africa has evolved significantly over the last two decades. Defining this evolution is the introduction of the concept of value-added in the revised definition (2000) of internal auditing. The role of internal auditing has expanded to include

services that add value not only to internal control processes, but also meet the needs of various stakeholders through embracing governance and risk management in their on-going efforts to achieve this.

Internal auditing in local governments of South Africa has the potential to add substantial value and to make a meaningful contribution in respect of governance, should the IAFs be empowered with the status required to enable them to meet the demands of today's changing environment. A survey conducted by the National Treasury (2014) identified three significant factors preventing IAFs in national departments and local governments from taking their rightful place as governance partners. These are the status of internal auditing within the departments and municipalities; the changing role of internal auditing, and the competencies of internal auditors and staffing policy requirements of the departments.

In addition to their responsibility for assessing and recommending internal controls, internal auditors' skills in risk management and their broad-based perspective of the organisation, uniquely position them as a valuable resource for strong corporate governance. As a result, informed senior managers and boards rely on internal auditors for advice and counsel on everything from analysis of operations and assessment of risk, to recommendations for improved corporate governance (IIA, 2013). Moreover, internal auditors are increasingly being challenged to apply their expertise in broader ways than ever before, such as evaluating emerging technologies, detecting and deterring fraud, analysing the effectiveness of policies and procedures, and identifying opportunities to save the resources of shareholders.

In conclusion, the introduction of the Public Finance Management Act (PMFA) (Act 1 of 1999) in 2000, with its focus on good governance and accountability (and which made internal auditing compulsory in the public sector), meant that internal auditing became a formal part of the financial management process in the South African public sector. This coincided with increased international recognition of the value of the IAF, as well as an expansion of the IAF's role from what had basically been an accounting-orientated service to a much broader, management-orientated service, and a true governance partner.

Despite the above stated need for and importance of the IAF, internal auditors in the South African public sector may be falling short due to failure to fully meet the expectations of their stakeholders. However, when it comes to adding value across the board, there's no better resource than internal auditing.

4.17 CONCLUSION

This chapter considered different views of the effectiveness of IAFs. From 2011 to 2017, various studies conducted on the effectiveness of IAFs produced diverse study results, and it was evident that these studies focused on different aspects/features, regarding the effectiveness of IAFs in various countries.

Based on the above discussions, the literature made clear that there are various views by various researchers on what constitutes the effectiveness of an IAF in any organisation. However, no study was found to focus specifically on the effectiveness of IAFs in South African municipalities, which prompted the need to conduct this study. The following chapter (Chapter 5) will discuss the methodology followed in conducting this study in order to address the problem statement in Chapter 1.

CHAPTER 5

RESEARCH DESIGN AND METHODOLOGY

5.1 INTRODUCTION

This chapter aims at providing the methods used and procedures followed by the researcher in providing a solution to the problem statement discussed in Chapter 1 of this study. To accomplish this objective, a literature review was conducted in order to determine the acceptable practices and roles which are expected of effective IAFs in municipalities in South Africa.

These roles and practices were tested through empirical research in this study, and were based on the secondary data obtained from the available literature and analysis of the audit reports presented by the Auditor-General South Africa (AGSA) as from 2011/2012 to 2015/2016. A content analysis method was used to analyse the data gathered from the AGSA reports, and this data was important in solving the study's problem statement.

The empirical research was conducted as follows: a detailed content analysis of the AGSA reports from 2011/2012 to 2015/2016 was done. This analysis covered the five-year period, which provided sufficient data and information to assist the researcher in formulating the framework for effective IAF. The AGSA analysis focused on the following:

- Ideal characteristics of an effective IAF;
- Roles and responsibilities of an effective IAF;
- Independency of IAFs in South African municipalities;
- Comments made by the AGSA on municipal IAFs in South Africa;
- Major weaknesses found by the AGSA in municipalities' IAFs;
- Recommendations by the AGSA on how IAFs can improve their functioning; and
- IAF trends from 2011/2012 to 2015/2016 in terms of improvement.

The AGSA reports analysis assisted the researcher in formulating an effective framework for use by internal auditors in performing their daily work. This chapter therefore explains in detail the design and methodology followed by the researcher in conducting the empirical study, including: the theoretical framework that guided this study; the research design; selection of the population and sample frame; the sample size; the sampling method and the data collection process; and the analysis of the primary data collected.

5.2 THE RESEARCH PARADIGMS

Research paradigms are seen and regarded “as a set of beliefs and practices that guide the researcher during the research process” (Ackermann, 2015; Harrits, 2011; Doyle, Brandy & Byrne, 2009). Doyle et al. and Ackermann argue that a specific paradigm is defined by the epistemology, meaning “how do we know what we know”; the ontology, meaning “the nature of reality” and axiology, meaning “the values of the researcher”. This set of beliefs places a researcher within three broad research paradigms namely, positivism (the quantitative paradigm), constructivism (qualitative paradigm) and pragmatism (mixed methods paradigm) (Ackermann, 2015; Harrits, 2011; Doyle, Brandy & Byrne, 2009).

Stahl (2007:4) defines the positivism paradigm as a research paradigm which is based on the ontological doctrine that reality is independent of the observer”. While ontological assumptions form the most important structural blocks of how the world is perceived (Stahl, 2007: 4), it is for this reason that Aliyu, Bello, Kasim and Martin (2014) associate the positivist paradigm with quantitative research. Alessandrini (2012) explains that the positivist favours quantitative data, while the non-positivist or constructivist paradigm favours qualitative data. According to this paradigm reality can be realised through analysis of numbers.

On the other hand, Alessandrini (2012) explains constructivism or the non-positivist paradigm as paradigm which rejects the positivist ideology. Non-positivism or constructivism emerged in reaction to the dominance of the positivist approach (Alessandrini, 2012): non-positivists or constructivists recognise that data collected through a positivist approach, such as empirical data, can be rendered invalid just because of its positivist treatment that includes the avoidance of opinion and speculation (Alessandrini, 2012). Hence, a positivist approach can be used in qualitative research (Aliyu, et al. 2014).

Thus, this study supported the constructivist paradigm for its determination, objectivity, reliability, and support of generality (Broom & Willis, 2007: 22). The study used a secondary source of information from Broom and Willis (2007: 22) and Motubatse (2016), who recognised that the use of secondary data through content analysis fits the constructive paradigm. The advantage of using the non-positivist paradigm or constructivist paradigm to answer the important research questions about IAFs in different types of municipalities in South Africa lies in its preference for opinions raised by the AGSA, and generalisation and objectivity rather than quantification and assumption.

The following sections explain the theoretical framework followed in this study in the context of the paradigms discussed above.

5.3 THEORETICAL FRAMEWORK

This study sought to develop a practical framework for an effective IAF in South African municipalities. The framework was focused on how the effectiveness in local government spheres could be improved in the future. Therefore, both the institutional theory and the agency theory were found to be the most suitable and relevant theories to be employed in order to achieve the research aims. The following is the discussion of both institutional theory and agency theory, and an explanation for combining them within this study.

5.3.1 Institutional Theory

According to Kraft's Public Policy (Kraft & Scott, 2007), an institutional theory is a "policy-making theory that emphasises the formal and legal aspects of government structures". Scott (2004) argues that the institutional theory is "a widely accepted theoretical posture that emphasises rational myths, isomorphism and legitimacy. Institutional theory focuses on the deeper and more resilient aspects of social structure. It considers the processes by which structures, including schemes, rules, norms, and routines, become established as authoritative guidelines for social behavior" (Scott, 2004).

Institutional theory further defines public administration as part of political life, and questions the assumption that state machinery functions as an indistinguishable whole and as a passive agent. Jean-Claude (2011: 12) asked why resources and power are allocated unequally in the public sector. According to the institutional theory, organisations such as municipalities are considered institutional actors in their field, promoting the values and interests which are rooted in the local communities in which they operate, and not just machines implementing goals and values defined by a principal. This theory further considers government as a business that forms its own environments, rather than adapting to existing environments. The theory argues that "public administration is driven by societal visions and political projects". Therefore, organisations such as municipalities that handle public affairs should be "conceptualised as institutions rather than as instruments" (Brunsson & Olsen, 1997: 20).

Furthermore, Scott (1995) claims that for organisations, including municipalities in South Africa, to survive, organisations should follow the rules and belief systems prevailing in their own

environments (Meyer & Rowan, 1977), because institutional isomorphism, both structural and procedural, will earn the organisation legitimacy (Suchman, 1995).

The literature indicates and suggests that prior research has used institutional theory to study internal audit related studies (Al-Twaijry, Brierley & Gwilliam, 2003; Arena, Arnaboldi & Azzone, 2006; Mihret, James & Mula, 2012). Institutional theory “focuses on aspects of social structure. It gives an explanation of how institutional patterns, structures and practices are shaped through coercive, copied and normative isomorphism (DiMaggio & Powell 1983). This is in line with the objectives of this study as it focuses on the effectiveness of IAFs in municipalities with special focus on what characterises this IAF and how stakeholders perceive these IAFs. The importance of institutional theory lies in what an organisation actually accomplishes and what their structures suggest to the external environment that they should accomplish (Kalbers & Fogarty, 1995). This is apparent in South Africa, as the municipalities are expected to function as per the MFMA and are established in terms of the country’s constitution. However, organisations may indicate that they are operating in line with the expectations of the external environment, while in fact they are not doing so (Meyer & Rowan, 1977)”. This is exactly what prevails in South African municipalities, where there are laws and regulations that all municipalities are expected to comply with in carrying out their mandate; however, as per AGSA reports, it is evident that such laws and regulations are in fact not being followed.

Institutional theory further argues that “organisations sometimes engage in decoupling. Al-Twaijry, Brierley and Gwilliam (2003) embraced the isomorphic perspective for investigating the development of IAFs in Saudi Arabia. They state in their study that they consider that “the actual operations of IAFs are decoupled from the expectations of how they operate, as stated in SPPIA”. Institutional theory provided a perspective regarding their study results, and it was concluded that the IAFs are not well developed in Saudi Arabia. It was further noted that Arena, Arnaboldi and Azzone (2006) used the institutional theory in their study on the development of the IAFs in Italy.

Therefore, institutional theory is considered appropriate for internal audit related research for the following reasons: Firstly, the theory includes a field that comprises internal audit practices, which are a part of organisational phenomena. Secondly, it assists to explain organisational phenomena without assuming a limited set of organisational goals compared to transaction cost theories, which are based on the assumption of shareholder wealth maximisation. Third, it could support audit research in countries such as South Africa where the market is underdeveloped (Mihret, James & Mula, 2012). Prior research suggests that institutional theory is valid and relevant in internal audit research both in developing countries (Al-Twaijry, Brierley & Gwilliam, 2003; Mihret, Mula & James, 2012) and developed countries (Arena, Arnaboldi & Azzone, 2006).

This theory, as explained above, was found appropriate for this study, and relevant in addressing the stated research problem in Chapter 1. It can be seen from the discussion above that institutional theorists assert that institutional environments such as governments can strongly influence the development of formal structures in organisations, such as IAFs. This study was therefore carried out on the foundations of and beliefs in this theory.

5.3.2 Agency theory

In the available literature, a number of researchers have written about the dynamics of the principal-and-agent relationship as a means to explain agency theory (Hannafey & Vitulano, 2013; Lopes, 2012; Zu & Kaynak, 2012; Basau & Lederer, 2011; Mahaney & Lederer, 2011). These researchers “discuss how the principal-agent relationship can be used to manage the delivery of services required and reduce problems faced by service recipients in the immediate locality of the agent. Agency theory has its origins in economic theory (Motubatse, 2016), and was suggested as a means to evaluate relationships between principals and their agents. Kivistö (2007:3) acknowledges its origin, but argues that agency theory is not only understandable in terms of the discipline of economics; it has relevance in various fields including accounting, marketing, political science, public administration and management”. Agency theory was first conceptualised in order to understand the relationship between principals and their agents (Droege & Spiller, 2009; Segal & Lehrer, 2012; Mitchell & Meacheam, 2011), and this type of relationship can be traced back at least to the third millennium BCE in the Near East. Recently, Jensen and Meckling (1976) defined agency as:

“...a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision- making authority to the agent. If both parties to the relationship are utility maximisers, there is good reason to believe that the agent will not always act in the best interests of the principal. The principal can limit divergences from his interest by establishing appropriate incentives for the agent and by incurring monitoring costs designed to limit the aberrant activities of the agent”.

According to Mitchell and Meacheam (2011: 151), agency theory can be used to understand various organisational activities such as those rendered at municipalities in South Africa. However, once appointed as agents, people and departments are often tempted to become opportunistic and to place their personal interests ahead of those of their principals (Segal & Lehrer, 2012). Within the context of this study, agency theory was used to examine which framework could be formulated to ensure that the IAFs within municipalities’ best serve their municipalities in South

Africa. Since agency theory is based on the concept that principals delegate their power to the agents, (Segal & Lehrer, 2012; Mitchell & Meacham, 2011) it is equally important to point out that the principals can sometimes reclaim their delegated authority and act on their own behalf. In its simplest statement, this theory or business philosophy holds that agents will not exploit or compromise their principals' interests (Miller & Sardais, 2011; Zu & Kaynak, 2012; Hannafey & Vitulano, 2013; Mahaney & Lederer, 2011; Lopes, 2012; Basau & Lederer, 2011). Its validity, however, is continuously challenged in South Africa. In the context of this study, municipalities are expected to establish the IAFs in accordance with the MFMA Act, and provide these IAFs with an environment and opportunity to perform their functions fully and without any interference. On the other hand, the IAFs are expected to add the required value to justify their existence to their principals, thereby being effective.

According to Hannafey and Vitulano, (2013) and Zu and Kaynak, (2012), agency theory was first conceptualised to understand the relationship between principals and their agents. Hence, the theoretical framework, when applied to public sector entities, splits when trying to distinguish between agents and stewards in the municipality situation (Motubatse, 2016). For example, if the municipal managers behave as agents, then they are expected to manage the municipality's resources, making use of municipal budget allocations (for services such as housing, water, sanitation, health, education, etc.) to improve the lives of the municipality's residents through effective service delivery.

This theory is "concerned with the relationship between the principal and the agent, which occurs when one person or entity referred to as an agent can make decisions on behalf of, or that impact on, another person or entity referred to as the principal. As is increasingly clear from the growing number of protests in South Africa, some municipalities are failing to use their basic service budgetary allocations either in full or appropriately (Motubatse, 2016). Therefore, at financial year end, the unused funds that should have provided basic services are often required to be returned to the National Revenue Fund, effectively resulting in a total loss in terms of rendering services to the local community (National Treasury, 2015).

It is further noted that this "relationship is made more complex because sometimes the agents are motivated to act in their own best interests rather than in those of the principals. In addition, there is often confusion as to who is the principal in the whole relationship: provincial and national governments, or tax and rate-payers and local residents" (Motubatse, 2016). It is for this reason that the agency theory assumes that managers, such as municipal managers, have goals that conflict with those of their principals, and that managers (agents) may be pursuing their own goals

even to the detriment of their principals. On the other hand, “the principals experience challenges in obtaining sufficient accurate information to assess some of their agent’s (manager’s) behaviour (Motubatse, 2016). For example, municipalities in South Africa (their management structures and procedures) are supposed to address problems that have typically existed between distant agents and principals”. Thus, municipalities are the established organs of state tasked with service delivery such as water supply to residents; address quality issues; build houses to reduce backlogs; and install and maintain sanitation services to their local communities. In most cases, municipalities are part of an intergovernmental collaboration or network of government departments attempting to improve the living conditions of the country’s citizens.

The principals in all spheres of government are increasingly concerned about the possibility of being exploited by their agents. Such doubts are fuelled in particular by poor service delivery in and by municipalities, as evidenced by the level of protests. So far, the literature suggests that the relationship between principals and agents in South African municipalities is weak as can be seen by the declining level of basic service delivery to citizens. The weakness of this relationship is due to a number of issues, including the fact that political considerations are frequently given precedence over the rule of law, and that personal reactions to disparities in society sometimes turn violent (Motubatse, 2016).

An agency theory describes the importance of “the agent-principal relationship, and how this relationship can be managed. In the municipality situation, the agents (councillors and employees) have an obligation to fulfil the expectations of their local communities. According to Mitchell and Meacheam (2011: 151), agency theory could be used to understand a variety of organisational activities. In terms of agency theory, the principals delegate their power to the agents (Segal & Lehrer, 2012; Mitchell & Meacheam, 2011) who can then act on behalf of their principals (Hannafey & Vitulano, 2013; Lopes, 2012; Zu & Kaynak, 2012; Basau & Lederer, 2011; Mahaney & Lederer, 2011). In a municipality situation the municipal managers are delegated by their municipal councils to deliver services to the local residents. For these managers to fully perform their duties, they rely on other important functions such as IAFs, which are expected to add value by evaluating how the municipal mandate is being discharged”. Clearly, the relationship between municipalities as principals and IAFs as agents is not fully defined, and that agents are not delivering what the principals expect.

Therefore, the agency theory together with the institutional theory, were best suited for this study to address the stated research problem in Chapter 1. Agency theorists assert that the agent-principal relationship, such as the relationship between municipalities and their residents, can strongly

influence the way in which other services and activities are delivered. This study therefore subscribed to the foundations and beliefs of these two theories, as can be seen in the following sections.

5.4 RESEARCH DESIGN

William (2006: 12) defines research design as the overall strategy that the researcher chooses to integrate the different components of a study in a coherent and logical way, thereby ensuring that the research problem is sufficiently addressed. This explanation is further supported by Kumar (2005), who states that the research design constitutes the blueprint for the collection, measurement, and analysis of data in a particular study. De Vaus (2001: 14) claims that the function of a research design is to ensure that the evidence obtained enables the researcher to effectively address the research problem logically and as unambiguously as possible. In social sciences research, obtaining information relevant to the research problem generally entails specifying the type of evidence needed to test a theory, to evaluate a programme, or to accurately describe and assess the meaning of an observable phenomenon.

This study followed an exploratory design. An exploratory design is described as the design conducted when there are few or no earlier studies to refer to or rely upon to predict an outcome. The focus is on gaining insights and familiarity for later investigation, which is done when the research problems are in a preliminary stage of investigation. Exploratory design is often used to establish an understanding of how best to proceed in studying an issue, or what methodology would effectively apply to gathering information about the issue (Albert, Durepos & Wiebe, 2010; Michael, 2002).

The goals of exploratory research are intended to produce the following benefits (Albert, Durepos & Wiebe, 2010):

- Understanding the basic details, settings, and concerns.
- Well-informed picture of the situation being developed.
- Generation of new ideas and assumptions.
- Development of tentative theories or hypotheses.
- Determination about whether a study is feasible in the future.
- Refinement of Issues for more systematic investigation and the formulation of new research questions.
- Develop techniques and the direction for future research.

Exploratory design studies inform the researcher about the following, among others: (Albert, Durepos & Wiebe, 2010; Michael, 2002).

- Assist the researcher to gain background information on a particular topic.
- Assist in addressing the research questions of all types (what, why, how).
- Provide an opportunity to define new terms and clarify existing concepts.
- Often used to generate formal hypotheses and develop more precise research problems.
- In the policy arena or applied in practice, exploratory studies help establish research priorities and where resources should be allocated.

Therefore, based on the discussion above, this study followed a qualitative sequential exploratory design in the sense that it attempted to review the available literature in internal auditing, understand the situation prevailing at IAFs in South African municipalities; generated new ideas and assumptions on value-adding and the effectiveness of these IAFs; developed a framework that could be used in the future to evaluate the effectiveness of the IAFs; and provided a basis for future studies. Therefore, all the benefits highlighted in the discussion above are in line with the benefits expected from this study, thus making an exploratory design the best choice to conduct this study.

5.5 TARGET POPULATION

As indicated above, the study followed an exploratory sequential approach, which means that the population for the study consisted of 285 AGSA reports provided to the 285 municipalities existing in South Africa over a period of five years, being the period 2011/2012 to 2015/2016. The empirical data was collected from sampling these reports, which made up the target population of the study

5.6 SAMPLING FRAME

The detailed content analysis of the AGSA reports played an important role in addressing the problem statement, as stated in Chapter 1.

5.7 SAMPLING METHOD

A random sampling method was employed to stratify the municipal reports, which were analysed into subgroups to ensure that every municipality in each group had an equal chance of being selected without bias. This type of sampling was easy to use and apply.

5.8 SAMPLE SIZE

The sample size of this study was 10% of the 285 AGSA municipal reports, being equal to 30 reports multiplied by five years, amounting to 150 reports that were analysed for the purpose of this study. These sampled AGSA reports were stratified into the three main types of municipalities existing in South Africa, namely, types A, B and C. The researcher then randomly selected reports to be analysed from each group or type. The sampling involved five reports being randomly taken from type “A” municipalities (out of a possible of eight reports), 10 reports randomly selected from type C municipalities (out of a possible of 47 reports) and 15 randomly selected from type B municipalities (out of a possible of 230 reports). The numbers used from the municipalities for this sampling were as at 31 December 2017.

Therefore, a sample size of 30 AGSA reports was analysed and multiplied by five years, being the period of the five years under study. This sample size was found to be in line with the sample sizes used and targeted by similar studies conducted in other countries. An example of such a study is that of Shewamene (2014) on the determinants of internal audit effectiveness in the public sector, being a case study of selected Ethiopian public sector offices, in which a sample size of 72 participants was targeted and used. Therefore, in this study a sample of 150 reports in total were analysed.

5.9 RESEARCH METHODOLOGY

A qualitative research methodology was followed in this research. Qualitative content analysis is one of the numerous qualitative methods used recently for analysing data and interpreting its meaning (Schreier, 2012). As a research method, “qualitative content analysis embodies a systematic and objective means of describing and quantifying phenomena” (Downe-Wamboldt, 1992; Schreier, 2012). As a requirement for successful content analysis, the data is condensed into concepts that describe the research phenomenon (Hsieh & Shannon, 2005) by creating categories, concepts, a framework, a conceptual system or conceptual map (Weber, 1990). As stated in chapter 1 above, the research question specifies what to analyse and what to generate (Schreier, 2012).

In this qualitative content analysis study, an abstraction process was formulated in which concepts were created. From the perspective of validity, this study reported on how the results were reached, for readers to clearly follow the analysis and resulting conclusions (Schreier, 2012).

In the qualitative content analysis, an inductive content analysis process was used, which involved three main phases: preparation, organisation and reporting of results (Elo & Kyngäs, 2008). The preparation phase consisted of collecting suitable data from the AGSA reports for content analysis, making sense of the data, and selecting the unit of analysis. The organisation phase “included open coding, creating categories, and abstraction (Elo & Kyngäs, 2008), and the reporting phase included a content description of the categories that were used to describe the phenomenon, using an inductive approach.

Atlas.ti software was used to analyse the data as obtained from AGSA reports.

5.10 DATA COLLECTION PROCEDURES

This section details the methodology used for the data collection, which, in this research was documentary or secondary archival data. Leedy and Ormrod (2013) explain that data collection process begins after the research problem has been identified and the research design described. Babbie and Mouton (2010: 76) explain data collection as “the assembly of numerical data for quantitative research, or textual data for qualitative research” (Flick, 2011: 11–12).

Thus, data is empirical evidence or information carefully collected in accordance with the needs of the procedures dictated by the research (Neuman, 2011: 9). This study collected pre-existing (or secondary) data. Hox and Boeije (2005: 593) describe secondary data as “data originally collected for a different purpose and reused for another research question”.

Secondary data is further defined as “data collected by others for their specific purposes, and made available through books, libraries, and websites, to a wider audience which includes researchers (Diamantopoulos & Schlegelmilch, 2004: 5; McCaston, 2005: 2; Adams, Khan & Raeside, 2014: 104), Such data includes information relating to government surveys and administrative records (Remler & Van Ryzin, 2011: 533; McCaston, 2005), which were originally organised to achieve other objectives (Hox & Boeije, 2005; Doolan & Froelicher, 2009; Johnston, 2014). McCaston (2005) explains that secondary data “with a research orientation” is widely sourced from research information collected by governments or large institutions”. For this research, the secondary data came from the publicly available data on the AGSA website. It included the audit outcomes reports for the 2011/2012 to 2015/2016 municipal financial years. According to Walliman (2005:242), once a source of data is identified, it can then be subjected to interpretation.

The justification for the use of secondary data is that it enables the researcher to “skip the grind-work”, and concentrate on essential data analysis and interpretation (Adams et al. 2014:105). According to Adams, et al. (2014: 106), a researcher should justify “why a secondary data source is relevant to their efforts in addressing the research questions”. Johnston (2014) agrees by stating that the decision to use secondary data must arise from its ability to address the research problem, and the researcher’s assessment that the data fits the research aim”. Thus, the aim of this research was to develop a framework for IAFs at municipalities in South Africa using the AGSA municipal financial reports from 2011/2012 to 2015/2016. South African local government audits are conducted by the AGSA as mandated by the constitution. This secondary data was therefore the most appropriate source of data to answer the research question, primarily because of the consistency of its collection over a long period of time (Doolan & Froelicher, 2009: 205), and which indicated the characteristics of an ideal IAF, opinions raised, interdependence, and reasons for a particular opinion, etc.

Secondary data was also chosen as a data source for this research, as “it reduces the data collection time (Doolan & Froelicher, 2009: 214; Windle, 2010: 323)”. It can be carried out in a significantly shorter period possible than when collecting primary data (in this instance, a five minutes download of each AGSA’s report on average, compared to the five-year period needed to prepare and collect the audit reports from the AGSA) (McCaston, 2005). “Existing data can be analysed and reused for different perspectives, and its reuse provides an opportunity to discover relationships not previously considered in the previous research (Smith, 2008: 328). According to Kimberlin and Winterstein (2008: 2282), the first consideration for deciding whether secondary data can be used or not is to verify that the data is set appropriately to measure the variables required to answer the research questions. If the second set of research questions can be sufficiently addressed, the secondary data can be a valuable source of information, knowledge, and insight into a broad range of issues and phenomena (McCaston, 2005).

5.11 APPROACH FOLLOWED AND THE DATA COLLECTION METHOD

5.11.1 Data collection method

Content analysis is defined as a “systematic, replicable technique for condensing many words of text into less content groups, based on the clear rules of coding (Krippendorff, 1980; Weber, 1990). Krippendorff (1980) offers a comprehensive definition of content analysis as, “any technique for making inferences by objectively and systematically identifying specified characteristics of messages”. Content analysis enables researchers to examine big volumes of data (such as the

AGSA reports in this study), with relative ease in a systematic manner (Krippendorff, 1980)". It can be a useful technique for allowing researchers to discover and describe the focus of individual, group, institutional or social attention (Weber, 1990). "It also allows for interpretations which can be validated using other methods of data collection. Krippendorff (1980) noted that "too much content analysis research is motivated by the search for techniques to deduce from symbolic data what would be either too costly, no longer possible or too obtrusive by the use of other techniques".

Content analysis is also useful for examining trends and patterns in documents such as the ones analysed in this study. For example, Stemler and Bebell (1998) conducted a content analysis of school mission statements to make some inferences about what schools hold as their primary reasons for existence. One of the major research questions was whether the criteria being used to measure program effectiveness (e.g., academic test scores) were aligned with the overall program objectives, or the reason for their existence". The method produced good results that can be relied on (Stemler & Bebell 1998).

In addition to the above, content analysis provides an empirical basis for monitoring shifts in public opinion. Data collected from mission statements projects in previous years can be accurately compared to data collected at some point in the future to determine if policy changes related to standards-based reform have manifested themselves in school mission statements.

Content analysis can be seen as a readily-understood, less expensive research method. It is a modest research method that doesn't require any contact with people, and therefore provides reliable results. Content analysis has become a powerful tool lately when compared with other research methods such as interviews, observations and the use of archival records (Elo & Kyngäs, 2008). It is very useful for analysing historical material, especially for documenting trends over time" thus being relevant for this study.

The use of this research method ensures easy reliability and is proved to be more objective. In comparison to all other research methods, content analysis scores highest regarding its ease of repetition. Usually, the materials can be made available for other researchers to use (Weber, 1990: 35).

The above-mentioned data collection method was found to be appropriate and relevant in conducting this study and delivering its empirical evidence. The available AGSA reports on their website are considered reliable, and were analysed. This data collection method was considered to be relevant and suitable to provide reliable results.

5.11.2 Approach followed

This study used the inductive approach as recommended by Thomas (2012). The aim of using an inductive approach is “to shorten raw written data into a brief, summary format; establish clear links between the evaluation or research objectives and the summary findings derived from the raw data; and develop a framework of the underlying structure of experiences or processes that are evident in the raw data” (Thomas, 2012). Thomas (2012) further states that “the general inductive approach provides an easily used and systematic set of procedures for analysing qualitative data that can produce reliable and valid findings”. The inductive approach provides a simple, objective approach for providing findings in the context of focused evaluation questions. This approach was found to be relevant and appropriate for this study and its nature. Therefore, the Atlas.ti software was used to analyse the secondary data and assisted in measuring the validity of the results that were translated in the form of a developed framework produced by this study.

5.11.3 Statistical analysis

The following statistical methods will be used on the empirical data sets:

5.11.3.1 Trustworthiness and credibility

To ensure the trustworthiness and credibility of data to be collected and analysed in this study the atlas.ti version 8 software was used for test analysis and building the framework developed by this study.

The General Inquirer as the classical package for content analysis studies was also used. This package was supplemented by using the Intext software as developed by Harald Klein for content analysis for the purpose of the trustworthiness and credibility of the results. These packages were used to supplement the analysis made by the Atlas.ti software mentioned above.

5.11.3.2 Descriptive analysis

In this study, data analysis was conducted in a three stage processes, namely, data reduction, data display and extraction of conclusions. The collected data was analysed using the packages and software mentioned above. These packages were undoubtedly proven to be reliable and providing the required validity as the results obtained can be repeated at time.

5.11.3.3 Significance tests

The differences in results due to the fact that the analysis was made from different types of municipalities existing in South Africa as explained above, was analysed using Atlas.ti software.

This was done to test whether the municipalities' capacity, resources, or other factors had any impact on the results of the study.

5.12 QUALITATIVE DATA AND ANALYSIS

The AGSA reports for all municipalities from 2011/2012 – 2015/2016 were obtained from various websites of various municipalities existing in South Africa. These were the most recent reports available as the 2016/2017 reports were only released later after this study has been conducted. These AGSA reports were uploaded on Atlas.ti software which was used to perform coding and analysis. Qualitative content analysis was used to provide a deep textual description of the functioning of the IAFs as presented in the AGSA reports. The AGSA reports were coded using both concept-driven and data-driven approaches. For concept-driven approach a coding frame was developed which was imposed on all sampled AGSA reports. This analysis focused on IAFs only applying the relevant coding scheme. Using this approach, the coding was done focusing on the following:

- What are the key characteristics of an ideal IAF?
- What are the responsibilities of an IAF?
- What are the expected roles of IAFs?
- How independent are the IAFs in South African municipalities?
- What are the key audit opinions provided to the municipalities in South Africa?
- What are the main weaknesses raised by AGSA in municipalities?

As explained by Schreier (2012: 59) the coding frame is guided by a specific study's research questions. Therefore, the coding exercise was done to enable a rich description of the above areas based on what was found in the AGSA reports. In order to collect data on the areas mentioned above the following coding scheme and methodological procedures were used.

5.12.1 Concept-driven coding scheme

The following coding scheme was imposed on AGSA reports to retain the focus of this study:

Table 5.1: Coding Scheme used

Focus area	Main categories	Code assigned in AGSA reports	Code descriptor and example
Key characteristics of an ideal IAF	characteristics	characteristics	Any statement or segment of text in the AGSA reports which indicates the characteristic of IAF.
The responsibilities of an IAF	responsibilities	responsibility	Any statement or segment of text in the AGSA reports which indicates the responsibility of IAF.
The expected roles of an IAF	roles	expected roles	Any statement or segment of text in the AGSA reports which indicates the role of IAF.
The independence of IAFs	independency	independence	Any statement or segment of text in the AGSA reports which indicates the independency of IAF.
Key audit opinions provided by AGSA	Opinions provided	opinions, unqualified, qualified, disclaimer and adverse	Any statement or segment of text in the AGSA reports which indicates the opinions provided.
Main weaknesses raised by AGSA	weaknesses	weaknesses	Any statement or segment of text in the AGSA reports which indicates the weaknesses.

Source: own research

These codes were developed based on the literature review discussed in Chapter 2 – 4 above and the research problem discussed in chapter 1 above. This approach of generating codes is called “concept-driven or deductive reasoning, as described by Schreier (2012: 60) and Ackermann (2015), in which data is obtained only from the focus areas of a study to solve the stated research question”.

5.12.2 Data-driven coding scheme

Apart from the coding scheme used in Table 5.1, the AGSA reports were scanned using Atlas.ti software to examine for any other segments of text regarding the IAF using the term “unit”. This helped the researcher, because if the data could not be categorised as per the above coding scheme (Table 5.1), the data was then coded inductively, or on the spot, as referred to by Ackermann (2015: 144). In this way, the functioning of internal audits departments in South African municipalities, as described in the AGSA reports, was obtained.

5.13 PROCESS FOLLOWED TO DEVELOP THE FRAMEWORK

In this study the developed framework was developed by study the available literature, and based on this literature review developed the categories and codes as indicated on Table 5.1 above. The main categories were identified as characteristics, roles, independency, responsibilities, opinions provided and weaknesses. This helped the researcher to focus and have a base to use during analysis of data. The reports were then analysed using atlas.ti software using the codes indicated. The findings were derived from the data, which together with the recommendations made by the AGSA were used to develop the framework for effective IAF. This means that the framework was developed as the result of the literature, the information obtained from the codes, the findings and the recommendations made by AGSA.

5.14 CONCLUSION

It is evident that this chapter serves as the main pillar for the entire research as it discusses the most important pillars of empirical research. It was highlighted in the discussion above that the study followed both the institutional theory and agency theory as its theoretical bases. It was discussed that a quantitative research methodology was followed, which was used to quantify the envisaged results. The study used the detailed content analysis of the AGSA audit reports, presented from 2011/2012 to 2015/2016. This assisted the researcher to track trends, comments, findings, and the recommendations made by the Supreme Audit Institution in South Africa, which then assisted in the development of an effective framework for IAFs.

The following chapter presents the results of the analysis made on the AGSA reports.

CHAPTER 6

FINDINGS, RESULTS, AND INTERPRETATION

6.1 INTRODUCTION

This chapter presents the empirical results of the study, and examines the qualitative results with reference to the problem statement discussed in Chapter 1. As discussed in the previous chapter, (Chapter 5) the empirical study of this research was twofold; firstly, a detailed analysis of the AGSA audit reports presented from 2011/2012 to 2015/2016 was done. This assisted the researcher in tracking the role and responsibilities of the IAF, the characteristics, independency, trends, comments, findings and recommendations made by the Supreme Audit Institution in South Africa. The first section of this chapter presents the findings and results of the analysis made on the reports of the Auditor-General South Africa using atlas.ti. Finally, based on the qualitative data and the results, the framework developed in this study of effective IAFs in municipalities in South Africa is presented.

6.2 QUALITATIVE FINDINGS OF THE AGSA AUDIT REPORTS AND THE ANALYSIS

The following sections provide a qualitative discussion of the effective IAF in municipalities in South Africa, regarding the following:

- Roles and responsibilities;
- Independence;
- Characteristics of effective IAF;
- Key AGSA findings leading to qualified opinions, disclaimer, and adverse opinions;
- Patterns and trends;
- Key recommendations made by AGSA in municipalities; and
- Challenges preventing the smooth running of the IAFs.

Sections 6.2.1 to 6.2.6 present the qualitative findings which were derived by using the concept-driven coding scheme explained in section 5.7 of chapter 5. Section 6.3 presents the framework developed from the qualitative findings.

6.2.1 Roles and responsibilities of IAFs in municipalities

Section 165 of the MFMA states the following roles and responsibilities that need to be performed by municipalities in South Africa:

Each municipality must have an IAF. Such IAF must:

(a) Prepare a risk-based audit plan and an internal audit programme for each financial year;
(b) Advise the accounting officer and report 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 this Act, the annual Division of Revenue Act, and any other applicable legislation; and

(c) Perform such other duties as may be assigned to it by the accounting officer”.

The MFMA further states that the IAF may be outsourced if the municipality requires assistance in developing its internal capacity, and the council of the municipality has determined that this is practical and economical.

Objective of analysis

To provide a text matrix on the number of municipalities per province in South Africa which were found to have the IAF in place for the period 2011/2012 to 2015/2016 financial years.

The findings

After the analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016 the following results were found.

6.2.1.1 Municipalities with established IAF per province

Table 6.1 shows the municipalities with established IAFs per province.

Table 6.1: IAFs established in municipalities per province:

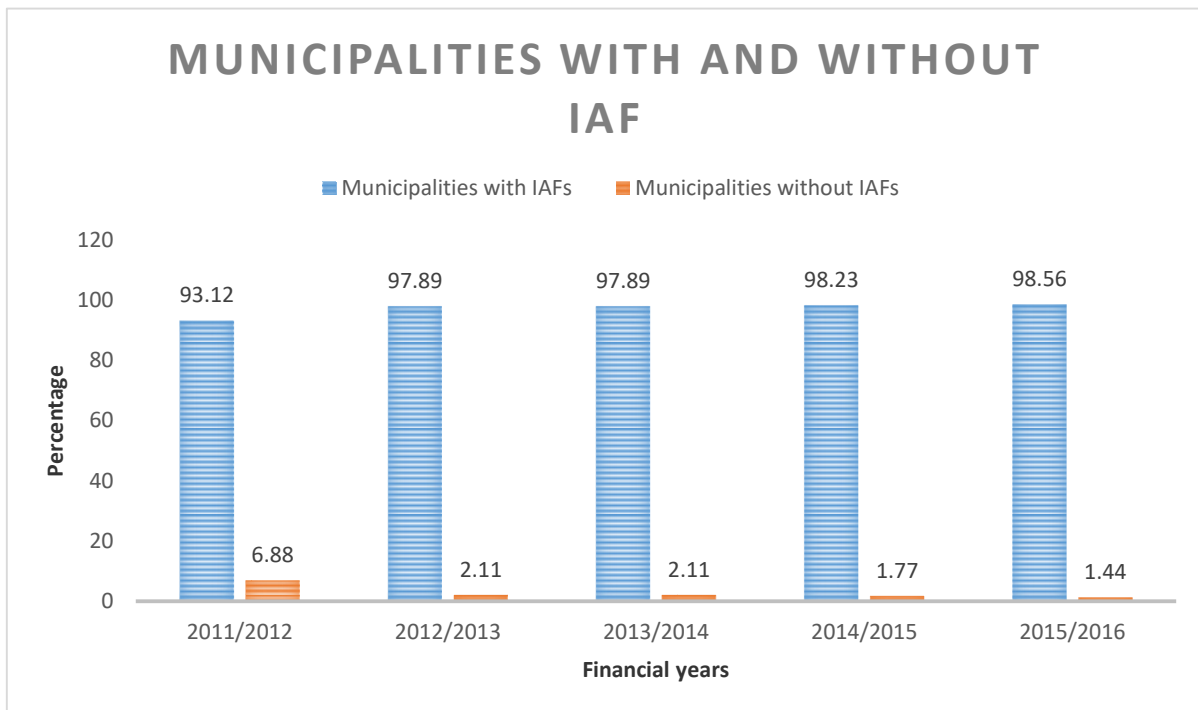
Province	Percentage of established IAF	2011 - 2012	2012 - 2013	2013 - 2014	2014 - 2015	2015 - 2016
Eastern Cape municipalities	Established IAF	95%	100%	100%	100%	100%
	Not in place	5 %	0%	0%	0%	0%
Free State	Established IAF	88%	100%	100%	100%	100%
	Not in place	12%	0%	0%	0%	0%
Gauteng	Established IAF	95%	100%	100%	100%	100%
	Not in place	5%	0%	0%	0%	0%
Kwazulu-Natal	Established IAF	97%	100%	100%	100%	0%
	Not in place	3%	0%	0%	0%	0%
Limpopo	Established IAF	97%	100%	100%	100%	100%
	Not in place	3%	0%	0%	0%	0%
Mpumalanga	Established IAF	100%	100%	100%	100%	100%
	Not in place	0%	0%	0%	0%	0%
North West	Established IAF	85%	88%	88%	91%	84%
	Not in place	15%	12%	12%	9%	16%
Northern Cape	Established IAF	86%	93%	93%	93%	93%
	Not in place	14%	7%	7%	7%	7%

Western Cape	Established IAF	92%	100%	100%	100%	100%
	Not in place	8%	0%	0%	0%	0%

Source: own research

In the 2011-2012 financial year, not all municipalities were found to have IAFs in place, although the percentage of those municipalities without the IAFs was found to be low, ranging from 3% to 12%. This means that these municipalities lacked an oversight function to assist their audit committees, if any, in providing an oversight role that would have assisted in identifying the potential risks and weaknesses. These municipalities can be further seen in Figure 6.1 below.

Figure 6.1: Percentage of municipalities with and without IAFs from 2011/2012 to 2015/2016



Source: own research

This finding paints the overall picture of the number of municipalities in South Africa which have the IAFs. The establishment of these IAFs as discussed above are important in ensuring that the municipalities and those in authority are assisted in their mandate.

6.2.1.2 Responsibilities of IAFs

Objective of analysis

To provide qualitative tests of the responsibilities that are expected to be undertaken by IAFs in municipalities in South Africa.

Findings

Table 6.2 provides an overview of the responsibilities of IAFs per province, as prepared by the AGSA for the financial years 2011/2012 to 2015/2016.

Table 6.2: Responsibilities of IAFs according to the AGSA

<p>Responsibilities of IAFs in municipalities</p>	<p>“The audit committees need to be resourced adequately to fulfil their roles and responsibilities, it must be highlighted that the effectiveness of an audit committee mostly depends on a properly resourced and skilled internal audit unit that produces timely, relevant and quality reports on the systems of internal control.</p> <p>“Furthermore, the auditees lacked effective management and leadership oversight; roles and responsibilities of all levels of staff were not clearly defined and management did not hold transgressors accountable”.</p> <p>“Audit committees and IAFs should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible”.</p> <p>“Audit committees and IAFs should assist by identifying breaches of legislation and reporting breaches to the leadership for action to be taken against those responsible”.</p> <p>“IAFs to identify risks and the controls that can be implemented to mitigate the risks”.</p> <p>“Audit committees and IAFs should assist councils to make informed decisions”.</p> <p>“IAFs should assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.</p> <p>IAFs should assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and</p>
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	<p>compliance with legislation.</p> <p>Audit committees and IAFs should assist by identifying breaches of legislation and reporting these breaches to the leadership for action to be taken against those responsible”.</p> <p>IAFs to identify risks and the controls that can be implemented to mitigate the risks”.</p> <p>“The IAFs of districts and local municipalities should be adequately capacitated with the skills to assist with actively following up on information technology commitments”.</p> <p>“Identifying gaps in the internal audit process which limit the amount of reliance that the AGSA can place on their work for external audit purposes and the role of the internal audit unit around performance information”.</p> <p>“A well-functioning internal audit unit can play a critical role in ensuring the credibility of financial and non-financial information used for decision-making purposes”.</p> <p>“IAFs are expected to advise municipalities on the internal controls that can be implemented to strengthen the control environment and ensure credible reports”.</p> <p>“IAFs should play a more effective role in tracking the progress made by municipalities in implementing management commitments in respect of previously raised audit findings”.</p>
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Source: AGSA reports

Based on the qualitative tests in Table 6.2 above, the following observations necessary for effective IAFs in municipalities were made:

- The IAFs should be properly resourced and skilled to produce timely, relevant, and quality reports on the systems of internal control within their municipalities.
- Should clearly define their roles and responsibilities and hold wrongdoers accountable.
- Should identify inconsistencies within their internal audit process to increase the amount of reliance that the AGSA can place on their work for external audit purposes, and the role of the IAF around performance information.
- The IAFs should help their councils to make informed decisions by providing guarantee that preparation documents and end-year reports on actual performance are trustworthy.

- The IAFs should assist accounting officers and management in the performance of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.
- The IAFs of districts and local municipalities should be sufficiently capacitated with the skills to assist with actively following up on information technology commitments.
- The IAFs and audit committees should provide credible reports to those in authority within their municipalities.
- The IAFs should make sure that their internal audit plans are aligned to the risks identified in their municipalities, and should specifically focus on those key controls directly affecting the credibility and accuracy of financial and performance reporting and compliance with laws and legislation regulations.
- The ACs and the IAFs should assist by identifying gaps in legislation and reporting these breaches to the leadership for action to be taken against those responsible.
- The IAFs should review the business processes and operational plans to ensure an improvement in daily operations and service delivery.
- A well-functioning IAF should play a critical role in ensuring the reliability of financial and non-financial information used for decision-making purposes.
- The IAFs are expected to advise municipalities on the internal controls that can be implemented to strengthen the control environment and ensure credible reports.
- The IAFs should play a more effective role in checking the progress made by municipalities in implementing management commitments in respect of previously raised audit findings.
- The IAFs should identify risks and the controls that can be implemented to mitigate the risks.

All these responsibilities as outlined in the AGSA municipal reports are in line with the roles and responsibilities expected from a well-functioning IAFs as per IIA requirements, as discussed in Chapter 2. It is therefore important for IAFs to have a complete framework that can be used to fulfil all their expected roles and responsibilities to ensure the smooth functioning of the municipalities and to fully add the value required.

A summary of the findings discussed above are presented in Figure 6.2.

Figure 6.2: Responsibilities of IAF in municipalities



Source: own research

Figure 6.2 can be interpreted as being per role and responsibility, as identified from the AGSA reports:

A functioning IAF should provide quality, relevant and timely reports. This means that the reports produced by the IAFs should be of quality, credible, and be given on time to assist the municipalities and those in authority to address challenges and problems timeously before experiencing any major impacts. The IAFs should further assist municipalities in providing

credibility on financial and non-financial information to support the municipalities in submitting their financial statements and other non-financial information such as statistics, in compliance with specific requirements such as those of GRAP, etc.

The IAFs should assist municipal councils in making informed decisions. It is important for every municipality and its management to make decisions that are informed as they have a mandate to deliver services to their citizens and therefore should always act in the best interests of the citizens. Functioning IAFs should assist in this regard by continuously investigating best practices on behalf on the municipalities and advise appropriately.

A functioning IAF should assist accounting officers to execute their duties. The MFMA requires that the IAF should be established to assist, among others, the accounting officers to perform their duties. This is possible if the IAF is staffed by skilled and competent personnel who know what to do and when.

A functioning IAF should ensure that its municipality is in compliance with laws and regulations that govern the running of the municipalities and its activities such as the MFMA and Treasury regulations etc. It is the responsibility of every IAF to fully study and become knowledgeable of all regulations that need to be followed by the municipality to fully comply with the laws surrounding the municipalities. The IAFs should further assist their municipalities in identifying breaches in legislation if any, and report them timeously to the municipality's management for correction.

A properly functioning IAF should ensure that the internal audit plans are aligned to the risks of their municipality. This is an important role because the IAF exists in municipalities to serve them and those in authority by identifying any risks to be faced. Therefore, in their audit plans, the IAFs need to align their plans to those of their municipalities and should further assist in identifying risks and the corrective controls that can be implemented to mitigate such risks.

A well-functioning IAF should assist its municipality in reviewing its business processes and operational plans. Municipalities are established to provide services to the people residing within the municipality. They do so by providing various services such as water supply, electricity, sanitation, roads, etc. It is therefore important for every IAF in a municipality to assist in reviewing its normal business processes and operational plans. This can be done by continuously evaluating whether the operational plans and business processes are of best practice and meet the citizens' expectations.

A well-functioning IAF should assist in tracking the progress made by the municipality in implementing previous findings. The findings raised previously by either the IAF or by the AGSA must be addressed to ensure that there is progress in the municipality regarding the area raised, and for ongoing development. The IAF should always track the findings that have been addressed, so that the challenges in those areas are not repeated.

Based on the findings and interpretation provided above, the following checklist is presented in Figure 6.3 for use by IAFs to self-check that they are complying with their responsibilities and adding value to their municipalities:

Figure 6.3: Checklist for IAF roles and responsibilities

Role and responsibilities checklist for an IAF:		
	Yes	No
Is the IAF submitting its reports timeously?		
Is the IAF adequately staffed with skilled and competent staff?		
Is the IAF reporting to the highest level of management in the municipality?		
Are the reports produced by the IAF of quality and credible?		
Are the decisions taken by the councils in your municipality influenced by your recommendations?		
Are the accounting officers in your municipality able to execute their duties with the help of the IAF?		
Is the IAF assisting the municipality to comply with laws and regulations?		
Are the IAFs internal audit plans aligned to the municipality's goals?		
Is the IAF assisting the municipality in identifying breaches of legislation?		
Is your IAF providing credibility in the financial and non-financial information of the municipality?		
Is the IAF engaged in reviewing business processes and operational plans?		
Is the IAF tracking the progress made by municipalities in implementing the previous findings raised by both the IAF and AGSA?		
Is the IAF Identifying risks and recommending internal controls that can be implemented to mitigate risks that face the municipality?		

Source: own analysis

Overall summary

A well-functioning IAF should undertake all the roles and responsibilities identified in Figure 6.3. It should be indicated that for IAFs to succeed in performing these responsibilities, the checklist suggested above (figure 6.3) should be used. This finding addresses one of the objectives of this study that states that: to determine the roles and responsibilities of an IAF within a municipality. The finding indicates clearly what the responsibilities of an effective IAF are.

6.2.1.3 Roles of the IAFs

Objective of analysis

To provide qualitative tests of the roles that need to be played by IAFs in municipalities in South Africa.

Findings

The following qualitative text in Table 6.3 provides an overview of the roles of IAF per province as set out by the AGSA for the financial years 2011/2012 to 2015/2016:

Table 6.3: Roles of IAF according to the AGSA for the financial years 2011/2012 to 2015 to 2016

Province	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016
Eastern Cape	<p>“The lack of adequate progress can be attributed to inadequate oversight by those charged with governance, a lack of consequences when audit findings are not resolved, and a lack of consistent monitoring by IAFs and audit committees of the progress made in implementing management commitments”.</p>	<p>“The leadership and governance structures should complement this by strengthening monitoring and oversight by IAFs to create a high-performance culture that promotes accountability”.</p>	<p>“Our audits also identified that the accounting officers and/or oversight bodies such as IAFs did not investigate the previous year’s irregular expenditure to determine whether any person was liable for the expenditure.</p> <p>Consequently, auditees did not determine whether the irregularities constituted fraud or whether any money had been wasted”.</p>	<p>“At some municipalities, well-resourced, effective IAFs have helped to improve internal controls and have had a positive impact on audit outcomes. We assessed that 48% of the IAFs (2013-14: 45%) had a positive impact on audit outcomes. The main reason for the lack of positive impact was failure by management to address internal audit findings”.</p>	<p>“Ineffective oversight and assurance provided by internal audit and audit committees due to capacity constraints and skills challenges Ineffective oversight and assurance provided by internal audit and audit committees due to capacity constraints and skills challenges”</p>
Free State	<p>“The IAFs and audit committees did not exercise</p>	<p>“IAFs were not always fully capacitated with skilled,</p>	<p>“Our audits also identified that accounting</p>	<p>Same as above</p>	

	oversight responsibility to ensure that internal controls were implemented and monitored”.	experienced staff. Although IAFs exist in most cases, the control environment will be compromised if their findings are ignored or not taken seriously, which ultimately reduces the level of assurance that can be placed on financial information and the control environment”.	officers and/ or oversight bodies such as IAFs did not investigate the previous years’ irregular expenditure to determine whether any person was liable for the expenditure”.		
Gauteng	“There is a need for robust oversight over reporting on predetermined objectives by IAFs and audit committees. The oversight bodies such as IAFs did not adequately review the IDPs to ensure that SMART principles were adhered to when developing objectives and targets”.	“Oversight bodies such as IAFs and audit committees need to further sharpen oversight roles to monitor the extent of non-compliance with legislation and drive accountability”.	“As required by the MFMA, it is crucial that accounting officers and/or oversight bodies such as IAFs investigate irregular expenditure in a timely manner to determine if any person was liable for the expenditure”.	Same as above	Same as above
Kwazulu-	“Management was not	“Capacity constraints and	“Of concern is that although	Same as	Same as

Natal	provided with adequate guidance from oversight bodies such as IAFs.	limited budgets further affect the ability of IAFs to conduct their audits in a manner codified by the Institute of Internal Auditors as the required supervision, reviews and training cannot take place as expected and therefore oversight role has been compromised”.	IAFs and audit committees were in place at most auditees, not all these structures had a positive impact on the control environment and the oversight role was not played”.	above	above
Limpopo	“The oversight bodies such as IAFs give insufficient attention to the implementation and enablement, enforcement and monitoring of compliance with legislation. As a result, municipalities continue to incur irregular expenditure and suffer from a poor internal control culture with inadequate emphasis placed on the prevention and detection of	“IAFs and audit committees were not continuously monitoring the progress made with the implementation of management commitments”.	“Our audits also revealed that the accounting officer and/or oversight bodies, at 12 auditees (39%), did not investigate the previous year’s irregular expenditure to determine whether any person was liable for the expenditure. Consequently, auditees did not determine whether the irregularities constituted	Same as above	Same as above

	deviation from SCM prescripts”.		fraud or whether any money had been wasted”.		
Mpumalanga	“In general, the oversight structures such as IAFs were ineffective, as they did not perform the required oversight work throughout the period and therefore limited assurance could be obtained from their activities”.	“Audit committees and IAFs should play an oversight role to ensure that IT risks are appropriately managed”.	“Although IAFs were in place, they did not provide sufficient assurance in the areas they are required by legislation to audit and report on. These areas correspond to our assurance mandate. This means that their inability to function at the required level, together with the inadequate assurance provided by senior management and the accounting officers, placed undue pressure on our audit teams”.	Same as above	Same as above
North West	“Some expenditure was not investigated, as the oversight bodies such as IAFs of the municipalities did not have	“Lack of oversight by those entrusted with this responsibility, which stems from vacancies, lack	“There should be robust oversight of reporting on predetermined objectives by internal audit and audit	Same as above	Same as above

	sufficient knowledge of the legislation”.	of performance management and slow response by leadership to the root causes of poor outcomes”.	committees”.		
Northern Cape	“Audit committees and IAFs were in place in 19 (86%) municipalities. However, at 15 (79%) municipalities, the established audit committees and IAFs were not making the desired impact on the audit outcomes and did not play an oversight role”.	“The oversight bodies such as IAFs were to a large extent neglecting their oversight responsibilities . The IAFs at 79% of the municipalities are not adequate and effective. It was further noted that IAFs are not adequately staffed and, where positions are filled, the officials lack the required skills. It is recommended that district municipalities implement effective shared IAFs that can assist the local municipalities with proper oversight”.	“The management and leadership of the municipality and those that perform an Oversight or governance function should work towards improving the key controls, addressing the root causes and ensuring that there is an improvement in the six key risk areas, thereby providing assurance on the quality of the financial statements and performance reports as well as compliance with the legislation”.	Same as above	Same as above
Western	“The relevant oversight	“Ineffective oversight and	“The strong oversight	Same as	Same as

Cape	functions vested in mayors, accounting officers, senior management, IAFs and audit committees should be better exercised to ensure the effective implementation of the action plans”.	assurance provided by internal audit and audit committees due to capacity constraints and skills challenges”.	provided by audit committees of the work of IAFs ensured that audit committees were able to advise and provide the required assurance to councils, mayors, accounting officers or authorities and senior management on internal controls, information systems, reliability of financial information, reliability of performance information and compliance with legislation and supply chain management regulations”.	above	above
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Source: AGSA reports

Based on Table 6.3, the following observations were made:

There is a lack of adequate progress within the municipalities due to inadequate oversight by the IAFs. However, the IAFs were not always fully capacitated with skilled, experienced staff to perform the oversight function effectively. The findings further revealed that the accounting officers and oversight bodies at 12 municipalities (39%) did not examine the previous year’s irregular

spending to determine whether any person was accountable for the spending. Subsequently, municipalities did not determine whether the abnormalities created fraud or whether any money had been wasted. Therefore, the oversight role has not been fulfilled within some municipalities. There should be robust oversight of reporting on predetermined objectives by internal audit and audit committees to ensure that the IAFs are functional and add the required value. Management was not provided with adequate guidance from IAFs on how their work should be performed, which is more as an insight role. Ineffective oversight and assurance provided by internal audit and audit committees due to capacity constraints and skills challenges, need to be addressed to ensure effective IAFs.

It should be indicated that the literature suggests that the following roles need to be played by every IAF to be fully functional and effective: oversight, deterrence, insight, detection and foresight, as discussed in Chapter 2 (section 2.7). It was noted from the AGSA reports that it places more emphasis on the oversight role than on any of the other roles recommended by the literature. It would be interesting to determine how the AGSA would like to see other roles played by IAFs in municipalities.

Summary

There are various roles expected from a functioning IAF, as discussed in Chapter 2 of this study. However, it has been noted that the AGSA values or considers the oversight role as the main and the most important role to be played by IAFs within their municipalities. This finding addresses one of the objectives of this study that states that: to determine the roles and responsibilities of an IAF within a municipality. The finding indicates clearly what the roles of an effective IAF are; refer to section 1.3.2 in chapter 1.

6.2.2 Independence of IAFs in municipalities

Objective of analysis

To provide a text matrix on the views of the AGSA with regard to the independence of IAFs within municipalities in South Africa.

The findings

From the analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016, it was established that:

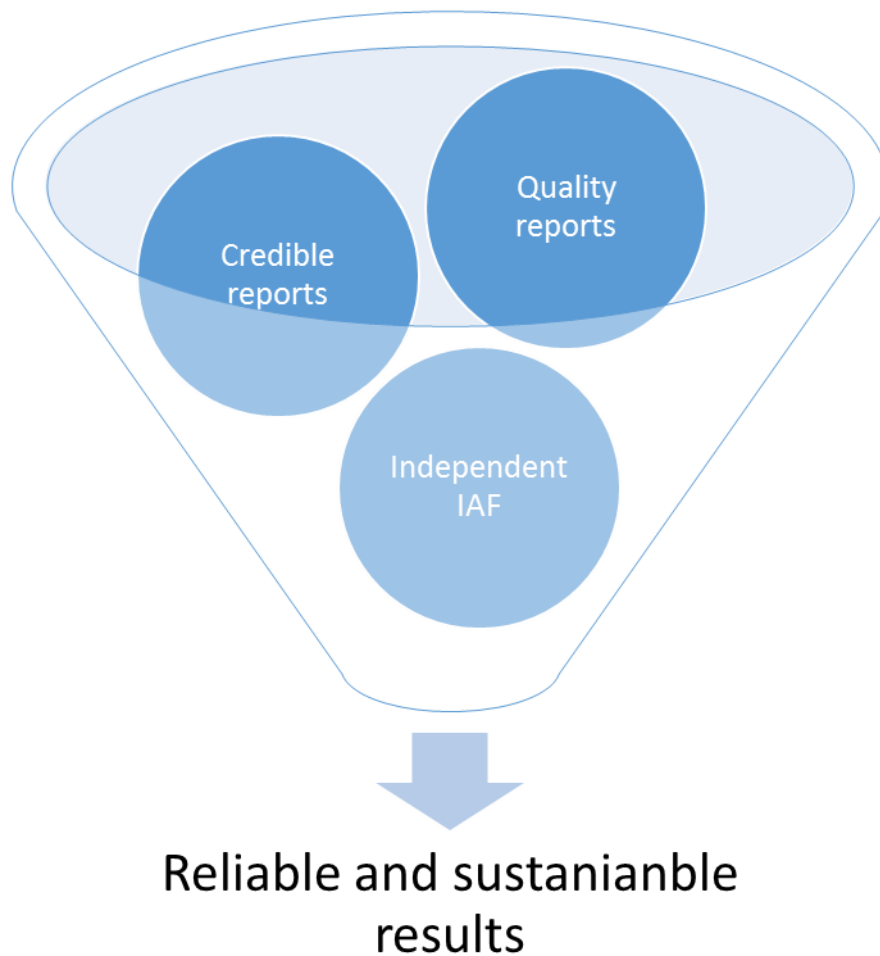
“IAFs did not have an appropriate, independent reporting channel and as a result could only provide limited assurance. Internal independent assurance and oversight as well as external independent oversight, needs to be significantly improve in order for quality, credible, reliable and sustainable outcomes to be realised”.

Source: *AGSA reports*

It was encouraging to note that independence issues of IAFs were not raised by the AGSA in many municipalities in the financial years 2011/2012 to 2015/2016. The IIA standard 1100 on independence and objectivity states: “the IAF must be independent and internal auditors must be objective in performing their work”. This standard emphasises the importance of the independence of the IAF in any organisation. Independence is interpreted to be the freedom from conditions that threaten the ability of the IAF to carry out internal audit responsibilities in an unbiased manner. This standard is further strengthened by the AGSA: “IAFs should assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation”. The above statements emphasise that for the IAF to successfully perform their work, they must work independently. Therefore, based on the qualitative extract in Table 6.3 above, the IAFs in municipalities were not provided with the appropriate and independent channel of reporting within the municipalities.

The importance of IAFs in municipalities is shown below in Figure 6.4:

Figure: 6.4: Role of an independent IAF



Source: own research

Figure 6.4 is summarised as follows: IAFs in municipalities need to provide quality reports that are reliable in order to obtain reliable and sustainable outcomes. If this process takes place, and IAFs are considered to be independent from management, they become valuable to the municipality. Therefore:

Reliable and sustainable outcomes = Independent IAF + quality reports + credible reports.

The formula is explained below as:

- Quality reports = reports that communicate the true state of affairs within the municipalities, which assists those in authority to take the necessary corrective action.

- Independent IAF = IAF that functions with objectivity and without restrictions and reports to the highest level of management.
- Credible report = reports that are trusted by those in authority because they were compiled without any bias.
- Reliable and sustainable outcomes = results that are valid and which can be achieved over time by the municipality.

Quality reports are reports that carry substance, are relevant, and take into account the municipality's environment. They should provide senior management with all relevant information needed to achieve their goals, mitigate risk, and comply with the laws and regulations.

Credible reports include unbiased and practical recommendations, and communicate the true state of affairs within a particular municipality.

Interpretation

The findings above, the information in Figure 6.4, and the formula for quality reports, it can be interpreted as follows:

Independence, as explained in standard 1100 of the IIA, is the most important aspect of any IAF. Independence is seen as the ability of the IAF, the CAE, or the internal audit staff to perform their duties in an unbiased manner. To accomplish the high degree of independence necessary to effectively perform the IAFs, the CAE, together with the entire internal audit staff, should have direct and unrestricted access to senior management and the board of directors. It should be stated here that any threats to independence within municipalities must be managed at all levels, namely: at the level of the individual auditor, and at the engagement, functional, and organisational levels. Objectivity is an impartial mental attitude that allows internal auditors to carry out engagements in such a manner that they believe in their work product and that no quality compromises are made. Therefore, independent IAFs and their staff are objective in their approach. Objectivity requires and suggests that internal auditors should not disclose their judgement on audit matters to others in any way. Therefore, threats to objectivity that may arise during internal audits must be managed at all levels.

The IAF must confirm to those in authority within the municipality, at least annually, the organisational independence of the IAF. The IIA further suggests in standard 1110.A1 that the IAF must be allowed to function without any interference whatsoever, in defining the scope of internal

auditing, performing audit work, and communicating results to the relevant parties (IIA standards), which is what is expected of all municipalities.

Therefore, the internal auditor's independence should be seen as a trademark of both the auditing and accounting professions. Independence should be viewed as the most important aspect of audited financial statements in protecting the interests of several parties, namely, management, investors, creditors, and the government.

The IAFs at municipalities should recognise the following three dimensions with regard to independence, which can assist IAFs to reduce threats:

1. Programming independence includes:

- Evading any managerial involvement with the audit programme at all costs;
- Evading any involvement with audit procedures to be performed; and
- Evading any review requirements other than the normal review that goes with the audit process.

2. Investigative independence, which should include:

- Clear access to all records, procedures, and employees relevant to the municipal audit;
- Complete support and cooperation from the municipality's management at all levels during the audit process;
- Independence to specify the scope of audit activities without the municipality's management involvement; and
- Independence from individual auditors' interests, which could lead to misstatements or the limitation of some audit processes due to self-interest.

3. Reporting independence, which should include:

- Providing internal audit reports without being forced to change the impact or significance of the audit findings;
- Providing reports without any force to omit important issues discovered during the audit;
- Evading intentional or unintentional use of unclear language in the statement of facts, opinions, and recommendations and in their interpretations; and
- Providing reports without fearing any override of the auditor's judgement regarding either

facts or opinions in the internal audit report.

This finding is inline with the section 2.12.2 and section 2.13 of chapter 2 that highlight the similar arguments with regard to independency of the IAFs.

This finding addresses one of the theoretical objectives of this study that states that: to discuss what must be considered in order to ensure independency of an IAF. And the finding further addresses the empirical objective that relates to analysing the AGSA reports to determine the independence of IAF in municipalities, refer to section 1.3.2 and section 1.3.3 in chapter 1 above.

6.2.3 Characteristics of IAFs in South Africa

Objective of analysis

To provide a text matrix on the views of the AGSA with regard to what characterises an ideal IAF in a municipality in South Africa.

The findings

On completion of the analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016, it was found that an ideal IAF should possess the following characteristics, as shown in Table 6.4 below.

Table 6.4: Characteristics of ideal IAFs (summary of the results)

Characteristic	Explanation
Competence - resourced and skilled competent staff	The IAF should be properly resourced and skilled and produce timely, relevant, and quality reports on the systems of internal control within their municipalities. The IAFs of both districts municipalities and local municipalities should be sufficiently resourced with skills to assist with actively following up on information technology commitments.
Assurance - assist those in authority to make informed decisions	The IAFs should help their councils to make informed decisions by providing assurance that planning documents and end-year reports on actual performance are trustworthy. A well-functioning IAF plays a crucial role in ensuring the trustworthiness of financial and non-financial

	information used for decision-making purposes.
Independent assurance - assist those in authority to execute their duties	The IAFs should help accounting officers and management in the performance of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.
Credibility - provide timely and credible reports	The IAF and ACs should provide reliable reports.
Recommendations - assist in risks identification and make practicable recommendations	The IAFs should make sure that their plans are aligned to the risks identified in their municipalities, and should precisely focus on those controls that directly impact on the reliability and accuracy of financial and performance reporting, and compliance with legislation regulations and the law. IAFs to identify risks and the controls that can be implemented to mitigate the risks.
Breach identification - assist in identifying breaches of legislation	ACs and IAFs should help by identifying gaps in legislation and report such gaps to the senior management for action to be taken against those responsible.
Review - assist in reviewing business processes and operational plans	The IAFs should review the business processes and operational plans to ensure an improvement in daily operations and service delivery.
Advisory - advise those in authority on internal controls	The IAFs should advise municipalities on the internal controls that can be implemented to strengthen the control environment and ensure credible reports.
Progress tracking - assist in tracking the progress made	The IAFs should play a more effective role in tracking the progress made by municipalities in implementing management commitments in respect of previously raised audit findings.
Assistance of external auditors - assist the AGSA to rely on their work	Should identify inconsistencies within their internal audit process that expand the amount of reliance the AGSA can place on their work for external audit purposes, and the role of the IAF around performance information.

Source: Own research

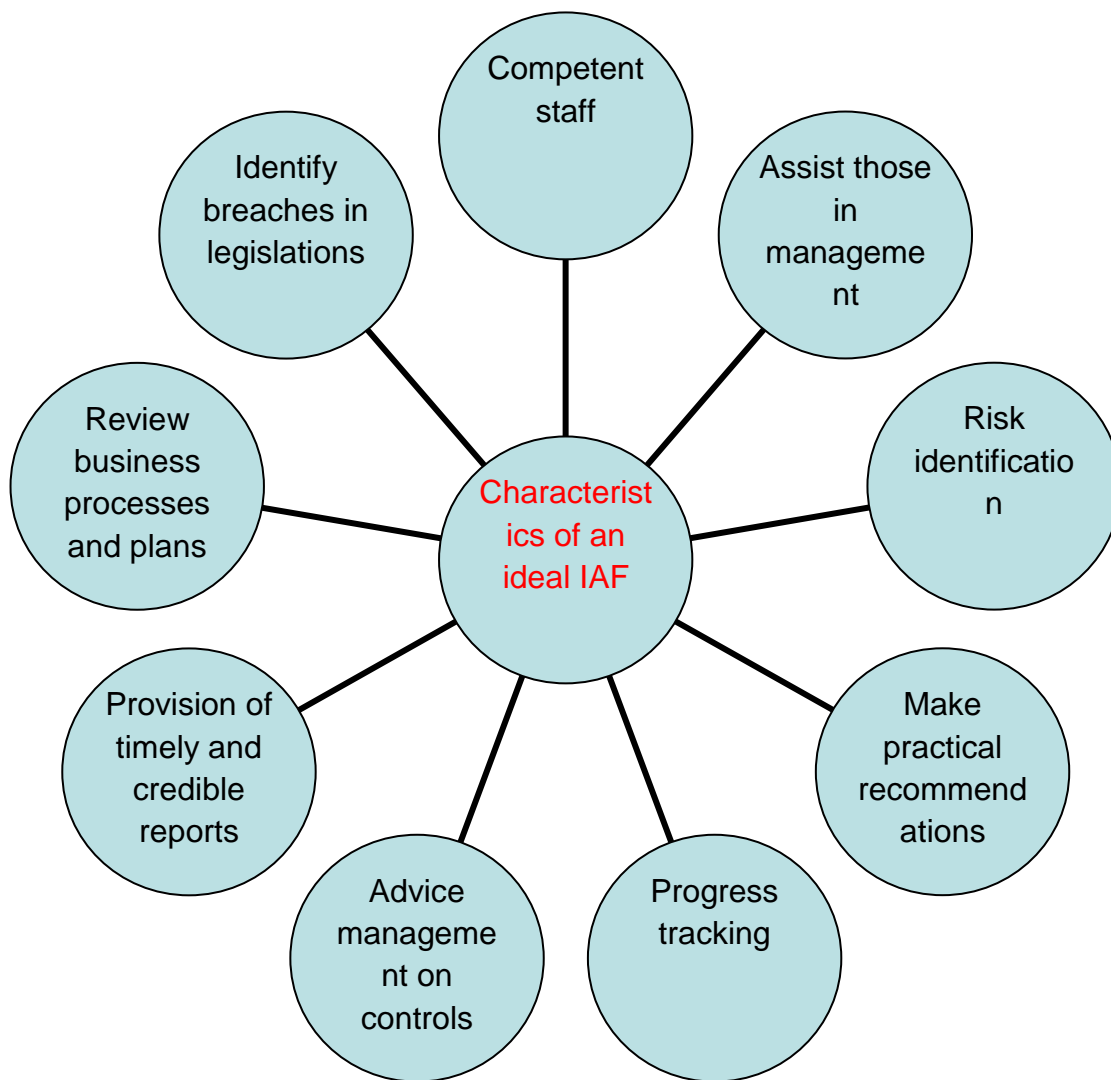
Table 6.4 reveals the following characteristics that are necessary for an ideal IAF to be functional and value adding:

A functional IAF should be adequately resourced and should be staffed with skilled competent staff who; assist management to make informed decisions and perform their duties; provide timely and credible reports; assist in risks identification and advocating practicable recommendations; assist in identifying breaches of legislation; assist in reviewing business processes and operational plans; advise those in authority on internal controls; assist in tracking the progress made; and assist the external auditors to rely on the work of the IAF.

Based on the deductions from Table 6,4 above, it is evident that an ideal IAF should possess a number of characteristics that, if properly applied by the IAFs, the IAFs will add value to their municipalities. These characteristics are in line with the characteristics of the IAF as suggested by the Institute of Internal Auditors. The question raised here, is do the current IAFs in municipalities possess these characteristics? If not, then a framework is necessary to bridge this gap.

Based on the deductions above, the following ten characteristics of a functioning IAF are shown in Figure 6.5 below:

Figure 6.5 Characteristics of a functioning IAF



Source: own research

This finding addresses one of the theoretical objectives of this study that states that: to identify the characteristics of an effective IAF. See section 1.3.2 of chapter 1.

6.2.4 Audit opinions provided by AGSA to municipalities

Objective of analysis

To provide a qualitative text on the types of opinions provided by AGSA to municipalities per province in the 2011/2012 to 2015/2016 financial years.

The findings and deductions

The analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016 indicated the following types of audit opinions provided to municipalities in South Africa:

The AGSA distinguishes between the different audits opinions it provides as follows:

Adverse opinion means that the financial statements contain material misstatements that are not confined to specific amounts, or that the misstatements represent a substantial portion of the financial statements.

Disclaimer audit opinion means that the auditee provided insufficient evidence in the form of documentation on which to base an audit opinion. The lack of sufficient evidence is not confined to specific amounts, or represents a substantial portion of the information contained in the financial statements.

Qualified audit opinion means that the financial statements contain material misstatements in specific amounts, or that there was insufficient evidence for auditors to conclude that the specific amounts included in the financial statements were not materially misstated.

Unqualified audit opinion means a clean audit opinion with no findings; this is given when all has been done as expected, and is in accordance with the laws and regulations. Table 6.5 shows the types of opinions provided.

Table 6.5: Types of opinions provided

Eastern Cape Province	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016
Unqualified opinion with no findings	0	0	2	7	7
Unqualified with findings	17	29	13	23	26
Qualified opinion with findings	20	12	17	20	18
Adverse opinion with findings	2	3	1	0	0
Disclaimer with findings	16	11	12	5	4
Free State					

Province					
Unqualified opinion with no findings	1	1	0	1	1
Unqualified with findings	8	8	12	13	15
Qualified opinion with findings	6	9	6	8	7
Adverse opinion with findings	0	0	0	0	0
Disclaimer with findings	11	8	9	3	2
Gauteng Province					
Unqualified opinion with no findings	2	3	13	15	16
Unqualified with findings	30	33	16	16	15
Qualified opinion with findings	6	2	2	2	2
Adverse opinion with findings	0	0	1	0	0
Disclaimer with findings	0	0	0	0	0
Kwazulu-Natal Province					
Unqualified opinion with no findings	1	9	20	22	22
Unqualified with findings	44	39	41	37	38
Qualified opinion with	9	10	8	8	7

findings					
Adverse opinion with findings	0	0	0	0	0
Disclaimer with findings	7	2	3	1	1
Limpopo Province					
Unqualified opinion with no findings	1	0	0	0	0
Unqualified with findings	1	1	15	12	12
Qualified opinion with findings	12	11	10	14	12
Adverse opinion with findings	1	1	1	1	1
Disclaimer with findings	14	7	6	6	5
Mpumalanga Province					
Unqualified opinion with no findings	2	1	2	2	2
Unqualified with findings	5	1	5	11	13
Qualified opinion with findings	7	11	8	6	5
Adverse opinion with findings	0	0	0	0	0
Disclaimer with findings	5	4	3	4	3
North West Province					

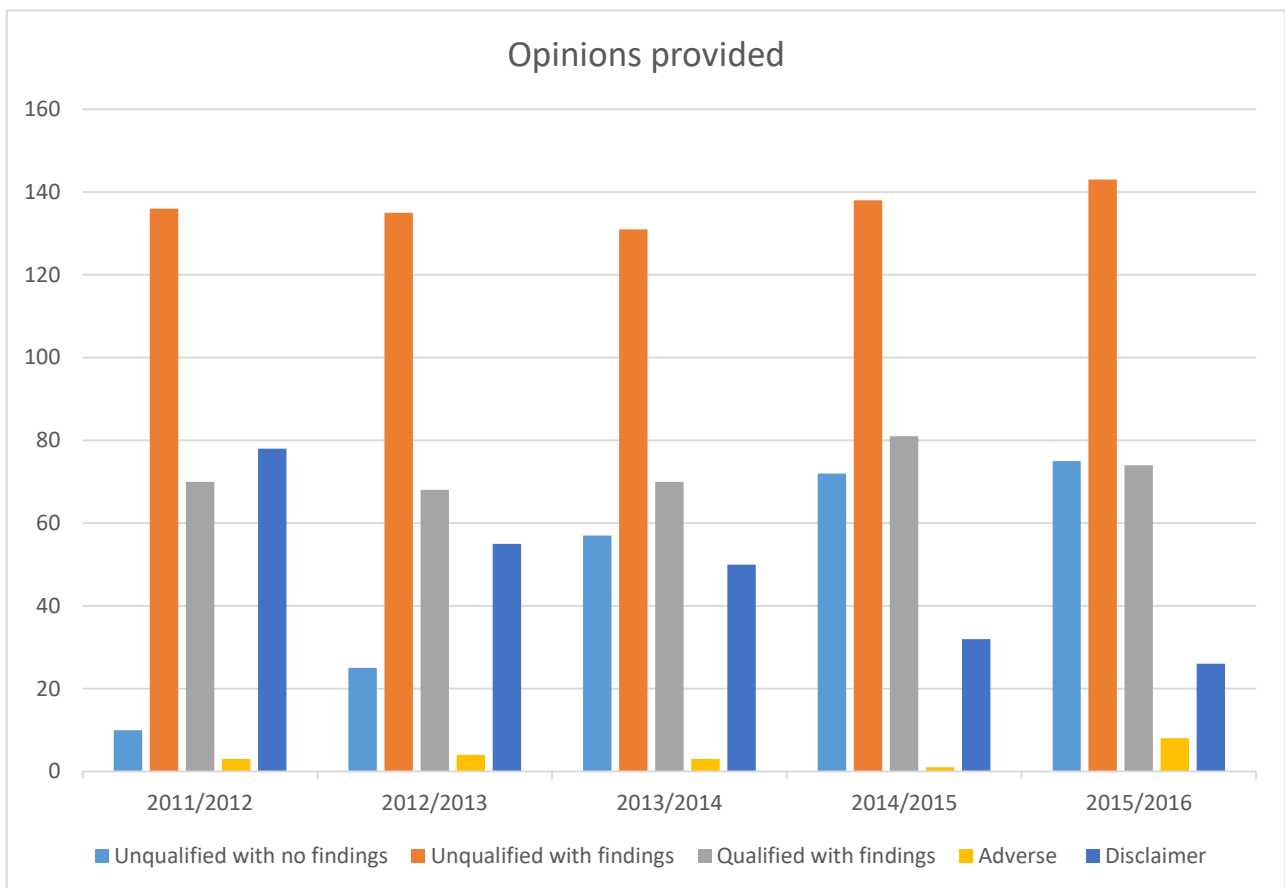
Unqualified opinion with no findings	0	0	0	0	0
Unqualified with findings	4	5	8	9	9
Qualified opinion with findings	3	6	9	10	11
Adverse opinion with findings	0	0	0	1	1
Disclaimer with findings	16	14	8	6	5
Northern Cape Province					
Unqualified opinion with no findings	0	1	2	2	2
Unqualified with findings	7	4	8	9	8
Qualified opinion with findings	6	6	10	13	12
Adverse opinion with findings	0	0	0	0	0
Disclaimer with findings	9	9	9	6	6
Western Cape Province					
Unqualified opinion with no findings	5	10	18	23	25
Unqualified with findings	20	15	14	8	7
Qualified opinion with findings	1	1	0	0	0

Adverse opinion with findings	0	0	0	0	0
Disclaimer with findings	0	0	0	1	0

Source: Own calculation from AGSA reports

Table 6.5 provided the actual number of opinions obtained by municipalities per province for the financial years 2011/2012 to 2015/2016. The findings in Table 6.5 above are further presented in Figure 6.6 below as follows

Figure 6.6: Opinions provided by AGSA to municipalities



Source: own research

Based on Figure 6.6 it is evident that a number of municipalities since the 2011/2012 to 2015/2016 financial years have received unqualified opinions with findings. One would expect to find these municipalities obtaining unqualified opinions with no findings, since most of them either have IAFs in place, or have the IAFs being outsourced to other firms. Figure 6.6 further indicates the number of municipalities that obtained disclaimer opinions, which means that these municipalities cannot provide the necessary documentation to support their financial statements, raising the question of

where these IAFs are in the municipalities, and what role do they play to ensure that this does not happen?

It is further evident from Figure 6.6 that the municipalities obtaining qualified opinions and adverse opinions remain constant, with no improvement. However, it is encouraging to note a declining trend, with municipalities obtaining disclaimers, the number declined from 78 in the 2011/2012 financial year to only 32 in the 2014/2015 financial year. Furthermore, the number of municipalities that obtained unqualified opinions with no findings improved from 10 municipalities in 2011/2012 to 72 municipalities in 2014/2015. Figure 6.7 demonstrates the numbers of unqualified opinions obtained per province between 2011/2012 and 2015/2016.

This finding addresses one of the empirical objectives of this study that states that: to analyse the AAGSA reports with the aim of determining the key findings leading to disclaimer and adverse opinions in municipalities in South Africa, refer to section 1.3.3 of chapter 1 above.

Table 6.6: Percentage of unqualified opinions received per province:

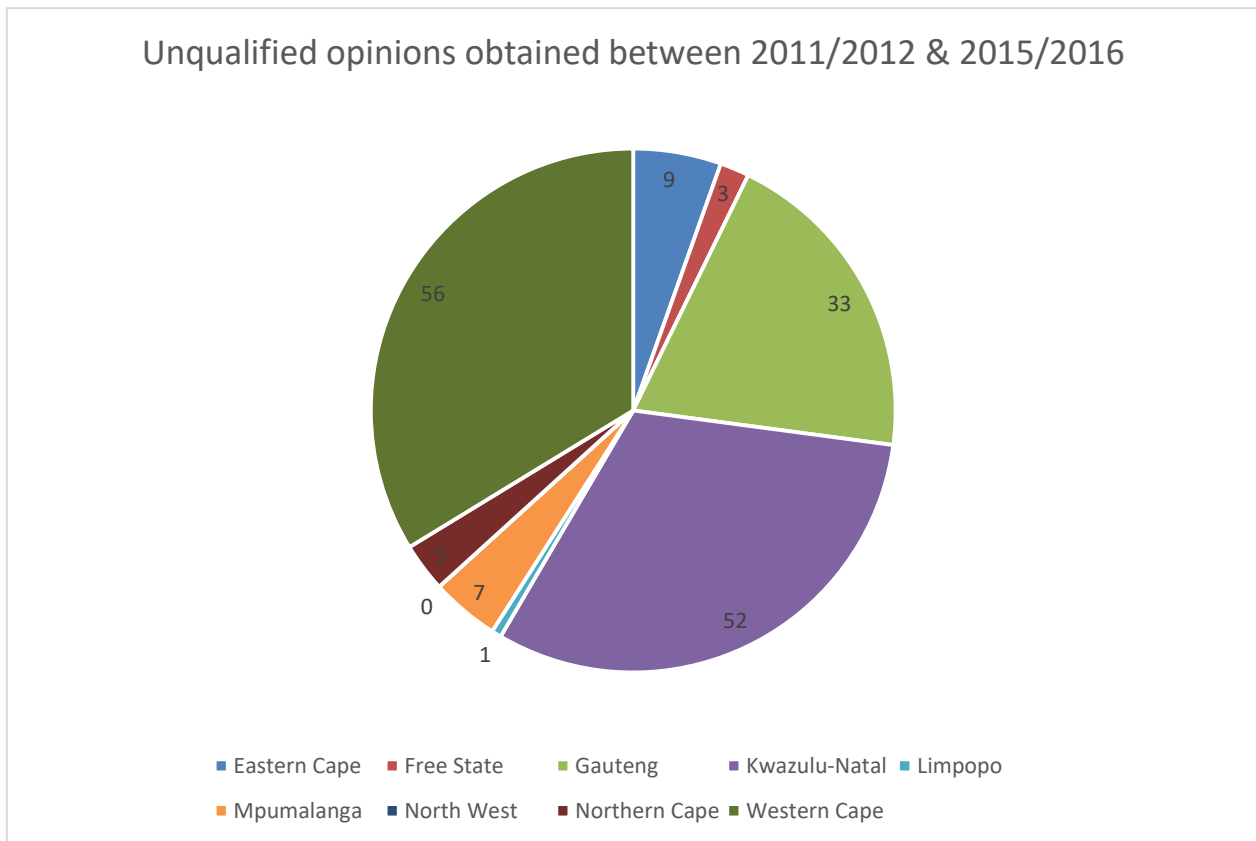
Province	Total number of municipalities	Unqualified opinions received from 2011/2012 – 2015/2016	Percentage of unqualified opinions in 5 years
Eastern Cape	45	9	4%
Free State	25	5	4%
Gauteng	12	33	55%
Kwa-Zulu Natal	62	52	16.8%
Limpopo	30	1	0.7%
Mpumalanga	21	7	6.7%
North West	23	0	0%
Northern Cape	32	5	3.1%
Western Cape	30	56	37%

Source: own calculation

Based on Table 6.6 above, the following deductions were made:

Municipalities are struggling to obtain unqualified opinions in many provinces including North West, Eastern Cape, Free State, Kwazulu-Natal and Northern Cape, with only municipalities in Gauteng and Western Cape performing better.

Figure 6.7: Unqualified opinions obtained per province:



Source: own research

Based on Figure 6.7 above, the following deductions were made:

That municipalities in the Western Cape have obtained unqualified opinions since 2011/2012 at a record 56 unqualified opinions. This is followed by municipalities in Kwazulu-Natal with unqualified opinions at 52, followed by municipalities in Gauteng at 33 unqualified opinions. It is noted from the analysis above that despite the North West municipalities having established IAFs; these municipalities have not received any unqualified audit opinions since 2011/2012. This trend is further seen in municipalities in Limpopo, where only one unqualified opinion has been obtained since the 2011/2012 financial year, and municipalities in the Free State province, where only three unqualified opinions have been obtained since the 2011/2012 financial year, until the 2015/2016 financial year. It is evident based on this information that the IAFs in these municipalities are not functioning and are not adding any value, therefore, a framework for IAFs to follow is crucial to bridge this gap.

6.2.5 Training of IAF staff members in municipalities

Objective of analysis

To provide a qualitative text on the training provided to IAF staff members in municipalities in the financial years 2011/2012 to 2015/2016.

The findings and deductions

The analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016 indicated the following types of training provided to IAFs staff members in municipalities in South Africa:

Table 6.7: Findings regarding training

“Personnel who do not have the required competencies are appointed in key positions, and that current employees do not keep up with the changing local government environment through ongoing training and development”.

“There is lack of oversight and training for new councillors. Councillors lacked the necessary training to perform their duties effectively and as a result did not fulfil the roles expected of them by legislation and the citizens of their constituencies”.

“Induction and training programmes need to be further refined by CoGTA and SALGA for these oversight structures to be effective”.

“In the past four years, we have consistently highlighted that for municipalities to improve their audit outcomes, they should have stability in key positions, invest in training programmes to ensure that the skills and competencies of staff (particularly in the finance unit) are enhanced, and institute consequences for poor performance and transgressions”.

“In collaboration with the provincial treasury, implement intensive training programmes to improve the skills of existing staff members to enhance their competence in performing their daily functions”.

“The employees to be trained were not identified or available to attend the training programme”.

“The lack of staff with minimum competencies and skills to perform their responsibilities was a root cause at 72% of the municipalities. This included employees that were appointed without the minimum competencies, current employees who did not keep up to date with ongoing training and development, and critical positions that were vacant and resulted in a skills gap”.

Source: AGSA reports

Based on Table 6.7 above, it is evident that training plays an important role in any organisation. This is supporting the literature discussed in chapter 4, sections, 4.6.2, 4.6.4 and 4.8 that discuss how important training of IAF and other staff is within a municipality. The municipal personnel were found to be inadequately trained and not available to attend training, even in areas where training

opportunities were made available. This culture needs to be changed. If municipal personnel attend training and continue to update themselves with current developments within their focus areas, the municipalities will then be able to comply with regulations and achieve their stated goals.

6.2.6 Key findings by AGSA with regard to municipalities

6.2.6.1 Key findings provided by AGSA

Objective of analysis

To provide a text matrix on the views of the AGSA regarding the key findings that led to qualified opinions in municipalities in South Africa.

The findings and deductions

Analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016 indicated the following, as shown in Table 6.7, as the main reasons for qualified opinions being provided to municipalities in South Africa:

Table 6.8: Key findings by the AGSA

Key findings	Root causes
Contracts awarded to suppliers in which employees or close family members of employees of the auditee had an interest.	“No process to verify credibility of information No, or limited, monthly reporting Lack of financial disciplines
Contracts that could not be audited.	Lack of knowledge of, or deliberate noncompliance with laws and regulations
Increase in irregular and unauthorised expenditure.	Lack of skills and readiness to address Generally Recognised Accounting Practice (GRAP)’s requirements.
Performance agreements not signed or performance management systems not in place.	Administrations not utilising the remedies at their disposal or required by rules and regulations. Inappropriate action plans or action plans not monitored adequately
Minimal assurance given by given by key role players such as IAFs.	Ineffective monitoring of commitments by oversight Audit committees not taken seriously
Audit committees and IAFs do not have positive impact.	Weak or understaffed IAFs”
Non-compliance with laws and regulations.	

Source: AGSA reports

Based on Table 6.8 above, a number of findings were raised by AGSA from the financial years 2011/2012 to 2015/2016, which ranged from non-compliance with laws and regulations, to increases in irregular and unauthorised expenditure, the irregular awarding of contracts, to lack of positive impact, by both the audit committees and the IAFs. All these findings were raised before the 2011/2012 financial year, with no tangible improvement despite having IAFs fully established in these municipalities. The IAFs are expected to assist their municipalities in various forms. According to the IIA on public sector auditing (2013:3-12), there are various roles expected to be played by internal auditors when performing their functions which include: oversight, detection, deterrence, foresight, and insight roles. Therefore, based on an extract from the findings in Table 6.7, the IAFs in municipalities seem not to be fulfilling these identified and expected roles, and thus are not functioning as expected.

6.2.6.2 Key findings by the AGSA regarding IAFs

Objective of analysis

To provide a text on the views of the AGSA regarding the key findings on IAFs in South African municipalities per province.

The findings

After concluding the analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016, the following main findings were raised with regard to IAFs in municipalities per province in South Africa. Table 6.8 presents these findings from the AGSA audit reports.

Table 6.9: The AGSA findings regarding IAFs per province in 2011/2012

Province	Financial year: 2011/2012
Eastern Cape	“While we have previously credited the province for the establishment of, and investment in, IAFs and audit committees, the impact of these role players on audit outcomes is fairly limited, as described in section 3.5 above. It is clear that the effectiveness of these structures is hampered by poor resourcing relating to the availability and competence of people serving in these structures and the lack of reaction to the work and reports of these structures by the level one assurance providers”.

	<p>“A lack of consistent monitoring by IAFs and audit committees of the progress made in implementing management commitments”.</p> <p>“Audit committees and IAFs were in place at 43 of the 45 municipalities in the province. They did not, however, have a positive impact on the audit outcomes for the year under review”.</p> <p>There were weak or understaffed IAFs”.</p>
Free State	<p>“A total of 24 (92%) auditees had audit committees and 23 (88%) auditees had IAFs. However, at 71% of the auditees the audit committees did not make any positive impact on the audit outcomes nor did internal audits have a positive impact on audit outcomes at 74% of the auditees”.</p> <p>“Limited or no assurance was provided by senior management, the municipal manager, mayor, council, IAFs and audit committees”.</p> <p>“IAFs did not include reviews of performance information systems and management or the internal audit reviews were limited as they did not focus on the usefulness and reliability of reported performance information”.</p> <p>“IAFs did not submit quarterly reports on its audits to the municipal manager and the performance audit committee [11 (42%) auditees”.</p> <p>A total of 15 (65%) IAFs did not meet all the legislated requirements”</p> <p>“IAFs did not evaluate performance information as part of their internal audit plans”.</p> <p>“A total of nine (38%) audit committees and six (26%) IAFs did not evaluate compliance with laws and regulations. Though audit committees and IAFs evaluate compliance, it was again noted that all (100%) municipalities had findings on non-compliance with laws and regulations”.</p> <p>“A17 (74%) IAFs were unable to positively impact on the audit outcomes”.</p> <p>“IAFs were not always fully capacitated with skilled, experienced staff. Although IAFs exist in most cases, the control environment will be compromised if their findings are ignored or not taken seriously, which ultimately reduces the level of assurance that can be placed on financial information and the control environment”.</p>
Gauteng	<p>“...IAFs and audit committees are not providing adequate assurance on</p>

	<p>compliance with supply chain management legislation”.</p> <p>“Inadequate monitoring of the work of consultants and ineffective oversight by governance structures, such as IAFs and audit committees”.</p> <p>“Audit committees and IAFs were in place at more than 95% of the auditees, but there was little impact on the overall audit outcomes”.</p> <p>“Lack of capacity and appropriate skills at IAFs”.</p> <p>“Lack of monitoring of implementation of action plans by IAFs and audit committees”.</p> <p>“There was still a lack of adequate quarterly reviews of financial and performance reports by IAFs and audit committees”.</p>
Kwazulu-Natal	<p>“Audit committees and IAFs were in place at 97% of the auditees, but at 36 auditees (53%) the audit committees were not making a positive impact on the audit outcomes. The same applies to IAFs, where there was little impact at 34 (50%) of the auditees”.</p> <p>“Ineffective monitoring by audit committees and IAFs”.</p> <p>“A total of 29% of the audit committees and 38% of the IAFs did not adequately evaluate the integrity and reliability of financial information. This resulted in a reduction in the level of assurance from these governance structures and is also indicative of regressions in the province”.</p>
Limpopo	<p>“Audit committees and IAFs were not fully compliant with legislative requirements, at 19 and 14 auditees, respectively”.</p> <p>“The lack of focus by IAFs on the audit of performance information also requires attention”.</p> <p>“IAFs and audit committees were not continuously monitoring the progress made with the implementation of management commitments”.</p> <p>“The IAFs at a number of auditees were also inadequately capacitated, which significantly impaired the level of assurance that they should provide”.</p>
Mpumalanga	<p>“Lack of consistent monitoring by IAFs and audit committees of the progress made in implementing management commitments”.</p> <p>“Audit committees and IAFs were in place at all municipalities, but at 15 (79%) of the auditees, the audit committees and IAFs did not have a positive impact on the audit outcomes, as their recommendations were not implemented”.</p>

	<p>“Ineffective monitoring by audit committees and IAFs”.</p> <p>“The internal control monitoring mechanisms of audit committees and IAFs did not function optimally, as many control weaknesses were only uncovered during the audit of the financial statements and compliance”.</p> <p>“Auditees’ risk assessment results did not inform the work plans of IAFs and the agendas of audit committees”.</p> <p>“IAFs at municipalities did not extend their scope to include IT audits”.</p> <p>“Audit committees and IAFs that are compliant with legislation is an important component of effective governance, risk management and internal control at the municipalities where they are appointed”.</p> <p>“Audit committees and IAFs did not broaden their scope of independent reviews to include all aspects of financial and performance management”.</p> <p>“Assurances given by IAFs on the adequacy of auditees’ systems of internal control were not supported by assessments undertaken in accordance with the International Standards on Internal Auditing”.</p> <p>“Although IAFs were in place, they did not provide sufficient assurance in the areas they are required by legislation to audit and report on”.</p>
North West	<p>“Audit committees and IAFs were established at 78% and 85% of auditees, respectively. However, at 81% of the auditees that have audit committees, the audit committees did not have a positive impact on the audit outcomes, while at 83% of the auditees the IAFs did not have a positive impact on the audit outcomes”.</p> <p>“The main areas in which IAFs were not compliant were as follows: no evaluation of internal controls, no evaluation of reliability/ integrity of performance information and no evaluation of compliance with laws and regulations”.</p> <p>“The main function of the internal audit is to review the internal controls at the auditees throughout the year and make recommendations to management and the audit committee for improvements. This was not done; hence the key controls at the majority of auditees did not improve during the year”.</p> <p>“The audit committees and IAFs did not appropriately evaluate the financial statements and the reliability of financial information at 52% and 22% of auditees, respectively. The audit committees and IAFs did not</p>

	appropriately evaluate the reliability of performance information at 52% and 22% of auditees, respectively”.
Northern Cape	<p>“Audit committees and IAFs were in place at 19 (86%) municipalities. However, at 15 (79%) municipalities the established audit committees and IAFs were not making the desired impact on the audit outcomes”.</p> <p>“Non-functional or noncompliant audit committees and IAFs and failure to implement proper control systems for safeguarding and maintenance of assets”.</p> <p>“District municipalities did not have proper systems and IAFs in place to perform the oversight function at local municipalities”.</p> <p>“The province was struggling to find sufficiently competent and experienced individuals to staff the IAFs in the province, which resulted in IAFs not having sufficient capacity to perform their required functions”.</p> <p>“Audit committees and IAFs at only four (21%) municipalities had a positive impact on the audit outcome of the municipality”.</p>
Western Cape	<p>“Audit committees were in place at all auditees, and IAFs were in place at 24 (92%) of the auditees, but at 13 (50%) of the auditees the audit committees were not making a positive impact on the audit outcomes”.</p> <p>“The continued ineffectiveness of the governance structures (IAFs and audit committees) at these municipalities as well as ineffective oversight by the municipal councils also contributed to the failure of the municipal leadership to submit financial statements within the legislated deadline”.</p> <p>“IAFs at municipalities did not extend their scope to include IT Audits”.</p> <p>“All the municipalities reported on had audit committees in place for the period under review, as prescribed by the MFMA. Two (8%) of the municipalities reported on did not have IAFs in place, contrary to the requirements of the MFMA”.</p> <p>“Non-compliance findings related to IAFs included the following: no/inadequate evaluation/advice or reporting on internal controls, accounting, risk and loss control, no reporting to audit committee on compliance with legislation, performance measurements not audited on a continuous basis, quarterly reports detailing performance against annual internal audit plan not submitted to audit committee, and no three-year strategic internal audit plan”.</p>

Source: AGSA reports

Based on Table 6.9 above, the 2011/2012 financial years were dominated by the following findings from the AGSA (in summary):

A larger number of findings emanating from the IAFs were raised in the 2011/2012 financial year, compared to all subsequent financial years. These findings raised were as follows:

Even though IAFs were well established in many municipalities, they did not contribute positively to the audit outcomes received by those municipalities, meaning that they did not add the expected value, and were therefore redundant. This finding was raised in all the provinces, as indicated in Table 6.8 above and dominated the findings raised by the AGSA. The root cause highlighted by this finding was lack of sufficient resources and competent, skilled internal auditors who would have assisted these IAFs to perform their functions optimally.

In performance of their functions, the IAFs did not include reviews of performance information or systems and management, or their internal audit reviews were found to be limited as they did not focus on the usefulness and reliability of reported performance information. Reviewing performance at municipalities is crucial, as the municipalities' primary mandate is to provide and deliver services to their communities. Therefore, the manner in which these services were delivered needs to be reviewed by the IAFs to ensure that necessary corrections are made. This finding linked directly with the finding that states that IAFs were found "lacking consistent monitoring of the progress made in implementing management commitments". It is important that the IAFs continuously monitor and report on the commitments made by the management of municipalities, and by so doing the IAFs will fulfil the important function of providing oversight on the work performed by those in authority, which is not the case as of now.

Table 6.9 further revealed that a number of IAFs in municipalities (varying from one province and municipality to another) did not evaluate their compliance with laws and regulations. This again indicates another important deviation and neglect of the IAFs in performing their fundamental function of ensuring and assisting their organisations, in this case municipalities, in complying with rules and regulations. The question that arises here is: what is the function of the IAF if it cannot assist its organisation in complying with laws and regulations as required?

Table 6.9 further revealed that the AGSA found many IAFs in municipalities were dysfunctional not compliant with the MFMA, and were failing to implement proper control systems for the safeguarding and maintenance of assets. One of the key responsibilities of the IAF is to assist

those in authority or management in safeguarding the assets of their organisations, and ensuring that those assets are protected from destruction and misuse.

It was lastly revealed that the IAFs did not comply with the following important areas outlined in the MFMA: inadequate evaluation/advice or reporting on internal controls; accounting; risk and loss control; no reporting to audit committees on compliance with the legislation; performance measurements not audited on a continuous basis; quarterly reports detailing performance against annual internal audit plan not submitted to audit committee; and three-year strategic internal audit plan. All these areas outlined here are key to every organisation and the IAFs are established to assist in achieving all those. However, the IAFs failed to make the contribution that was expected from them.

The following section provides the findings made by the AGSA regarding IAFs for the financial year 2012/2013. The information was used to determine if there were improvements in the findings or not, and whether the IAFs managed improvements in the poor areas mentioned above. Table 6.9 provides the AGSA findings.

Table 6.10: The AGSA findings regarding IAFs per province in 2012/2013

Province	Financial year: 2012/2013
Eastern Cape	<p>“The regression in governance can be attributed to the lack of staff with the necessary skills and competencies in the IAFs”.</p> <p>“While we previously credited the province for the establishment of, and investment in, IAFs and audit committees, the impact on audit outcomes and the assurance provided by these very important role players have been fairly limited. It is clear that the effectiveness of these structures is hampered by poor resourcing relating to the availability and competence of people serving in these structures and the lack of reaction to the work and reports of these structures by the assurance providers on the first level”.</p>
Free State	<p>“IAFs were in place at all auditees at an estimated cost of R33,7 million. However, these units were not yet providing the extensive assurance required and there had been a regression since the previous year. The operations of 66% of the IAFs were not fully compliant with the requirements of the Municipal Finance Management Act and the work of most of the units did not cover all the required aspects”.</p>
Gauteng	<p>“While audit committees improved their processes, the risk and IAFs within the auditees remained stagnant. This was mainly due to capacity challenges within IAFs and the skills required not being at a satisfactory level. This was mainly due to capacity challenges within IAFs and the skills required not being at a satisfactory level”.</p>

	<p>“Budgetary constraints also hampered the functioning of IAFs, resulting in them not reviewing or auditing critical processes such as predetermined objectives and compliance with legislation. Despite having fully staffed IAFs, some auditees outsourced the services of internal audit to compensate for the lack of appropriate skills”.</p> <p>“Integrated risk assessment processes and strategies were not adequately aligned to the IAFs’ initiatives, leading to internal audit activities not responding adequately to critical areas of concern such as compliance and the credibility of financial information”.</p> <p>“Both the audit committee and IAFs did not provide the required level of assurance with regards to the predetermined objectives”.</p>
Kwazulu-Natal	<p>“The level of assurance provided by internal audit decreased from 52% (2011-12) to 44% (2012-13). Some assurance is provided by 47% and limited or no assurance is provided by 7% of IAFs”.</p>
Limpopo	<p>“IAFs were not adequately resourced and audit committees were not overseeing and supporting their operations”.</p>
Mpumalanga	<p>“The operations of most IAFs complied with relevant legislation. However, our assessment indicates that only 14% had a positive impact on the audit outcomes. Inadequate resourcing of IAFs and management failing to implement internal audit recommendations continued to weaken the effectiveness of these units”.</p>
North West	<p>“The IAFs did not provide the required level of assurance and there has been no movement since the previous year”.</p> <p>“Three auditees (11%) did not have IAFs, while at the remaining auditees, internal audit services were mostly shared services per district. However, at two auditees (8%) the IAFs had a positive impact on the audit outcomes. At 63% of auditees, material non-compliance was identified with regard to the operation of the IAFs”.</p> <p>“We noted that in 42% of instances IAFs did not evaluate the reliability of financial information, in 46% of instances IAFs did not evaluate compliance with legislation and in 63% of instances IAFs did not evaluate the reliability of performance information”.</p> <p>“Even in those instances where the IAFs did focus on these key areas, management did not appropriately address the weaknesses identified by them”.</p>
Northern Cape	<p>“The IAFs at 79% of the municipalities are not adequate and effective. It was further noted that IAFs are not adequately staffed and, where positions are filled, the officials lack the required skills. It is recommended that district municipalities implement effective shared IAFs that can assist the local municipalities with proper oversight”.</p>
Western Cape	<p>“There has been significant improvement in the work performed by IAFs and</p>

	audit committees. However, at many auditees the leadership is still not taking the work of internal audit and audit committees seriously as they do not exercise sufficient oversight of the implementation of action plans to address both external and internal audit findings, which led to many repeat findings”.
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Source: AGSA reports

Table 6.10 above provided the findings raised by AGSA regarding the weaknesses picked during the financial year 2012/2013. Firstly, when comparing the 2011/2012 findings raised with the 2012/2013 financial year there is significant decline in the number of weaknesses raised, however, a thorough analysis is required to measure the impact of these findings raised in 2012/2013 with regard to the contribution that can be made by IAFs in their municipalities.

It is encouraging to find that the AGSA found significant improvement in the work of the IAFs in some provinces and municipalities. However, the most concerning and dominating finding was that the leadership, or those in authority in many municipalities, were not taking the work of the IAFs seriously, resulting in the AGSA repeating the same audit opinions and findings. An important question that needs to be raised here is why are the senior management of municipalities not taking the work of the IAFs seriously? How can municipalities spend millions of Rands annually in staffing and establishing the IAFs, while not taking the work done by such units seriously? Or is this done for compliance reasons? This study aimed to answer to these questions by providing a framework to be used by IAFs in municipalities to ensure that their work is taken more seriously.

In 2012/2013 financial year the findings on inadequate resourcing of IAFs were still found to dominate the findings, as in 2011/2013. Senior management in municipalities possibly does not see a good reason for having to provide the IAFs with sufficient resources. It is up to the IAFs to prove to senior management through good work that they should exist, and reasons why they should exist. Table 6.10 presents the findings regarding IAFs per province in 203/2014.

Table 6.11: The AGSA findings regarding IAFs per province in 2013/2014

Province	Financial year: 2013/2014
Eastern Cape	“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.

Free State	<p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p> <p>“These role players also did not insist on strong controls to ensure compliance with key legislation and to prevent, detect and correct material misstatements”.</p> <p>“IAFs at 67% of auditees provided limited/no assurance”.</p>
Gauteng	<p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p>
Kwazulu-Natal	<p>“Of concern is that although IAFs and audit committees were in place at most auditees, not all these structures had a positive impact on the control environment. This originated from the lack of understanding and appreciation by management of the importance of implementing recommendations and action plans of IAFs and audit committees”.</p> <p>“Risk assessments performed by IAFs did not get the buy in from senior management to fill gaps in internal controls”.</p>
Limpopo	<p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p> <p>“IAFs provided limited or no assurance at 43% of auditees, while the audit committees at 29% of auditees provided limited or no assurance”.</p>
Mpumalanga	<p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p> <p>“The internal audit unit did not include asset audits in their audit work, despite weaknesses in this regard having been previously reported. Where IAFs raised findings, management did not implement their recommendations”.</p> <p>“The capacity and focus of IAFs require immediate intervention, as these units are struggling to properly analyse risk and direct their scope of work to these areas, which directly affects the value added by the audit committees”.</p> <p>“Even though all municipalities had IAFs and audit committees, these role players are not yet providing the required level of assurance to have a positive effect on the audit outcomes”.</p>
North West	<p>“IAFs had not been established at 22% and audit committees at 33% of these auditees”.</p> <p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p> <p>“What is especially concerning is the instances where there are no audit committees or IAFs established at municipalities. Despite these assurance providers’ focus to comply with legislation, 41% of the established IAFs and 68% of the established audit committees did not fully comply with legislation”.</p>
Northern Cape	<p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p> <p>“IAFs had not been established at 10% and audit committees at 30% of</p>

	<p>these auditees”.</p> <p>“IAFs provided limited or no assurance at 67% of auditees. In total, 22% of these auditees did not have audit committees, while the audit committees at 45% of the auditees provided limited or no assurance”.</p>
Western Cape	<p>“The IAFs and the audit committees did not add to the credibility of financial statements reports, while monitoring and oversight by the political leadership did not have the desired results”.</p> <p>“There has been significant improvement in the work performed by IAFs and audit committees. However, at some auditees the leadership is still not taking the work of internal audit and audit committees seriously, as shown by the inadequate oversight of the implementation of action plans to address both external and internal audit findings, which has led to repeat findings”.</p> <p>“We are concerned that in some instances IAFs are drawn into the operations of the municipality, which impacts independence and oversight”.</p>

Source: AGSA reports

Table 6.11 above provides the findings raised by the AGSA regarding the weaknesses seen during the financial year 2013/2014. The IAFs were found not adding enough credibility on financial statements reports. This means the IAFs did not review and make corrective comments on the financial statements prepared by municipalities’ management. This function if properly performed could have assisted the municipalities to correct their financial statements before submitting such statements for external audit. Therefore, the IAFs need to be capacitated and resourced to ensure that they deliver all the expected services in order for them to be seen relevant and adding the required value. Table 6.10 shows the findings regarding IAFs per province in 2014/2015.

Table 6.12: The AGSA findings regarding IAFs per province in 2014/2015

Province	Financial year: 2014/2015
Eastern Cape	<p>“Internal audit plans did not sufficiently address significant risk areas, while planned audits were not performed due to cash flow challenges at some auditees”.</p> <p>“The assurance provided by audit committees and IAFs has declined on average by 12% since 2013-14 for the reasons mentioned in the assessment of governance key controls above”.</p> <p>“The assurance provided by IAFs and audit committees has improved over the past four years, as these assurance providers have identified areas of improvement in their municipalities. Unfortunately, senior management has been slow in implementing their recommendations, resulting in their efforts and value-adding contributions not yielding the desired impact of strengthening the internal control environment.</p> <p>The absence of IAFs and audit committees at 17% and 20% of municipalities, respectively, remained a concern (2013-14: 10% and 23%)”.</p>
Free State	Same as above

Gauteng	Same as above
Kwazulu-Natal	Same as above
Limpopo	Same as above
Mpumalanga	Same as above
North West	Same as above
Northern Cape	Same as above
Western Cape	Same as above

Source: AGSA reports

One of the findings raised by the AGSA regarding the functioning of the IAFs, was that the assurance provided by the IAFs in previous financial years has declined, which raises an important question: what causes IAF performance to regress or decline? IAFs are established in accordance with the MFMA requirement to assist their municipalities in different ways, with the ultimate goal of helping to improve performance.

It was found that IAFs were not properly addressing significant risk areas, and planned audits were not being performed due to cash flow challenges in some municipalities. Significant risks are important, and if not addressed, municipalities could collapse. It is expected of every effective and functioning IAF to help those in authority to identify such risks, and make realistic recommendations. Through its foresight role, this is supported by the IIA, which states that that internal auditors are expected to assist their organisations in being proactive by identifying business trends and bringing them to the attention of those in authority, along with appropriate recommendations for improvement to successfully deal with these challenges. Based on the qualitative text provided in Table 6.7 above, the IAFs were found to be failing in delivering this important role. The findings regarding the IAFs were found the same across all the provinces; this could be due to the standard auditing methodology and working papers used by AGSA.

Table 6.13 shows the findings regarding IAFs per province in 2015/2016.

Table 6.13: The AGSA findings regarding IAFs per province in 2015/2016

Province	Financial year: 2015/2016
Eastern Cape	“The municipality did not introduce appropriate mechanisms, processes, procedures, systems or internal controls to ensure that transactions are correctly recorded, classified, reconciled and reported on in accordance with SA standards of Generally Accepted Accounting Principles (GRAP). In cases where the municipality used the consultants, the consultants were not adequately monitored to ensure that their work were completed on time to allow the municipality to review and properly process that work in the financial statements. The IAFs and audit committees did not adequately review the accuracy, adequacy and reliability of the financial statements”.
Free State	“The audit committees did not promote accountability and service delivery by evaluating and monitoring responses to risks and providing oversight over the effectiveness of the internal control environment, including financial and performance reporting and compliance with regulations as limited reports were provided to them by the IAFs”. The audit committees were found not functional in some municipalities as they did not function for a major part of the financial year as a result, the internal audit departments did not report on any part of its work”.
Gauteng	“The AGSA did not identify any significant deficiencies in internal control”.
Kwazulu-Natal	“There was inadequate review of financial reporting and compliance with applicable regulations by audit committees and internal audit departments resulting in internal controls not preventing, detecting, and correcting material non-compliance”.
Limpopo	“There was slow response by management to implement the recommendations made by the internal audit departments”
Mpumalanga	“Management did not ensure that there were properly staffed and functioning IAFs throughout the financial year”. “The IAFs and audit committees did not adequately review the financial statements and performance reports”.
North West	“The IAFs were only operational for three months of the year in some municipalities”. The IAFs did not assist their municipalities with risk assessment nor with the compilation of action plans to address prior years findings”.
Northern Cape	“The audit committees were found not functional in some municipalities as they did not function for a major part of the financial year; as a result, the internal audit departments did not report on any part of its work”.
Western Cape	“The AGSA did not identify any significant deficiencies in internal control”.

Source: AGSA reports

It is encouraging to see that no undesirable findings were found by the AGSA in Gauteng and the Western Cape municipalities, which shows good improvement in these two provinces. However, other provinces still experience serious challenges with their IAFs, as these IAFs were found not to be functioning at all, or functioning for limited periods during the financial year, thus adding no value to their municipalities. There are further indications that in some municipalities, the IAFs do not comply with the regulations. This leads to the question the roles are these IAFs fulfil in their municipalities, and what value, if any, they add if they do not assist in this regard.

Summary of findings

The AGSA specifically states that the IAFs in municipalities do not adequately evaluate internal controls and therefore, do not fully advise or report to the audit committees on such matters such as accounting, risk management and loss control (Auditor-General South Africa, 2011: 32; Auditor-General South Africa, 2012: 86; Auditor-General South Africa, 2013: 31, 35, 75, 103). This fact is evident from the above discussion.

Based on Tables 6.8 to 6.12, the main finding raised by the AGSA over the past five financial years has been that while IAFs are established in many municipalities, their existence does not add any value, or very limited value, due to under staffing, incompetence, and lack of skills.

Although the AGSA audit reports show a decline in findings raised regarding IAFs as from 2011/2012 to 20115/2016, there are still of findings raised, that if properly addressed, will allow the IAFs to be functional and add the value expected by the MFMA, the IIA and the public. Therefore, a complete framework is needed that will take into account all the AGSA findings, and if properly followed, will ensure that IAFs in municipalities will comply, thus avoiding repetitive findings from the AGSA.

This finding addresses one of the empirical objectives of this study that states that: to analyse the AAGSA reports with the aim of determining the key findings leading to disclaimer and adverse opinions in municipalities in South Africa, refer to section 1..3.3 of chapter 1 above.

6.2.7 Key recommendations made by the AGSA regarding IAFs in municipalities

Objective of analysis

To provide qualitative data of the AGSA key recommendations to IAFs in the municipalities per province in South Africa.

The findings

Once the analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016 were done, the following main recommendations were made to IAFs in South African municipalities per province, as seen in Table 6.14:

Table 6.14: Key recommendations made by AGSA in 2011/2012

Province	Financial year: 2011/2012
Eastern Cape	“Audit committees and IAFs should be used proactively to assist the province in building the ethical culture required to ensure sustainable compliance with laws and regulations. In executing its duties, the audit committee assists the accounting officer in the effective execution of his or her responsibilities, with the ultimate aim of ensuring that the auditee achieves its objectives. IAFs are an integral part in providing assurance on governance, risk management and internal control”.
Free State	“IAFs should form an integral part of providing assurance on governance, risk management and internal control. IAFs need to evaluate key controls and assess the impact and corrective action required”.
Gauteng	“In addition, governance structures such as audit committees and IAFs should intensify their reviews of quarterly reports and monitor actual achievements compared to targets and track corrective action. The credibility and reliability of performance information is of critical importance as it enables full and effective oversight by the council and provides reasonable assurance to the council about attainment of service delivery objectives. Audit committees and IAFs should proactively assist in building the culture of accountability and ownership to ensure sustainable compliance with laws and regulations.”
Kwazulu-Natal	“The audit committees and IAFs need to take the following steps to improve audit outcomes: Arranging a joint planning session with external audit to improve cooperation and coordination throughout the audit process.

	<p>Ensuring that internal audits are conducted in compliance with the Internal Audit Standards.</p> <p>Ensuring that the internal audit is fully resourced by staff and technology.</p> <p>Ensuring that the internal audit plan is completed.</p> <p>Ensuring that all actions taken have a strong regard for independence and objectivity with the aim of achieving sustainable improved audit outcomes.</p> <p>Escalating the management cooperation to executive mayors and councillors”.</p>
Limpopo	<p>“The audit committee, as part of the governance structure of the municipality, must be in a position to determine the nature and extent of a formal review of the design and implementation and effectiveness of internal controls that should be carried out by the internal audit unit”.</p>
Mpumalanga	<p>“To improve audit outcomes, audit committees and IAFs need to review financial statements before they are submitted for auditing. They should also ensure that measures have been implemented to correct the previous year’s audit findings, and monitor the action plans to address audit findings. IAFs should insist on receiving monthly financial and performance statements. They should ensure that proper accounting records are kept, that all transactions are timeously processed throughout the financial year, that key reconciliations are periodically prepared, and that the accuracy of information is independently verified. IAFs should play an important role in monitoring the implementation of action plans. IAFs at municipalities should extend their scope to include IT audits. Assurances given by IAFs on the adequacy of auditees’ systems of internal control should be supported by assessments undertaken in accordance with the International Standards on Internal Auditing.”</p>
North West	<p>“IAFs should form an integral part in providing assurance on governance, risk management and internal control”.</p>
Northern Cape	<p>“IAFs should form an integral part in providing assurance on governance, risk management and internal control”.</p>
Western Cape	<p>“The relevant oversight functions vested in mayors, accounting officers, senior management, IAFs and audit committees should be better exercised to ensure the effective implementation of the action plans”.</p>

Source: AGSA reports

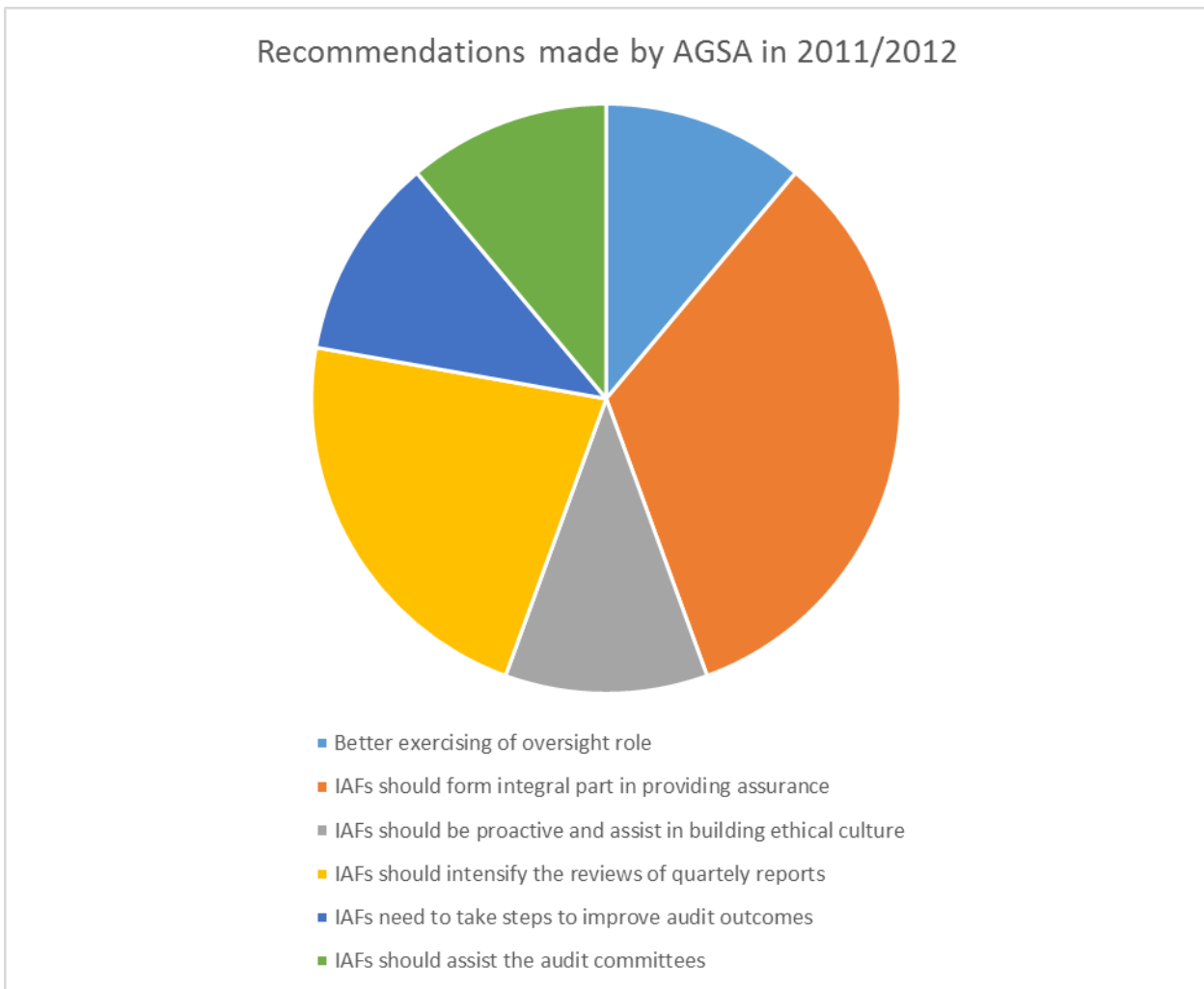
Based on Table 6.14 above, the following recommendations emerged as the most important recommendations that the AGSA made to municipalities:

The IAFs should be proactively to assist the province in building the ethical culture required to ensure sustainable compliance with laws and regulations. This recommendation places an important responsibility on IAFs within municipalities to ensure that a culture of compliance with the laws and regulations prevails within the municipality. The IAFs are expected to form an integral part of providing assurance on governance, risk management and internal control. This is done by evaluating key controls and assessing the impact and corrective action needed to add the required value within the municipalities.

The municipalities, through their accounting officers and audit committees, are required to ensure that the IAFs are fully resourced with staff and technology; ensure that the internal audit plan of the IAF is completed; and ensure that all actions taken have strong regard for independence and objectivity, with the aim of achieving sustainable improved audit outcomes. The AGSA further expects IAFs to review the financial statements prepared by the municipalities more often, to ensure that errors are detected and rectified on time and before such financial statements are submitted for external audit by the AGSA. All these recommendations can only be fully implemented through the use of a framework that considers all aspects needed for an IAF to function. This study therefore developed a framework to assist IAFs in complying with these recommendations.

The data presented in Table 6.14 is illustrated in Figure 6.8 below:

Figure 6.8: Recommendations made by the AGSA in 2011/2012



Source: own research

The Figure 6.8 above, provides the overall picture painted by the AGSA with regard to what IAFs need to do in their municipalities that they are not currently doing. The recommendation repeatedly given is that IAFs should form an integral part in providing assurance in their municipalities. This recommendation suggests that IAFs need to play a leading role in providing assurance to their municipalities, for this being a function that justifies their existence. Section 2.7 of chapter 2 above and table 2.1 above discussed the roles the IAFs should play in the municipalities to add the required value. A clear framework of AGSA recommendations was therefore developed, as shown in Table 6.15 below; to guide how these recommendations can be implemented.

Table 6.15: Key recommendations made by AGSA in 2012/2013 per province:

Province	Financial year: 2012/2013
Eastern Cape	“IAFs should assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation”.
Free State	“In executing its duties, the audit committee assists the accounting officer in the effective execution of his or her responsibilities, with the ultimate aim of ensuring that the auditee achieves its objectives”.
Gauteng	“The audit committees and IAFs of districts and local municipalities should be adequately capacitated with the skills to assist with actively following up on information technology commitments. Local municipalities should leverage from the information technology policies and procedures developed by district municipalities”.
Kwazulu-Natal	“IAFs should assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation”.
Limpopo	“IAFs should be adequately resourced and audit committees must oversee and support their operations. There are role players in local government, other than the external auditors, that are also required to contribute to assurance and confidence by ensuring that adequate internal controls are implemented to achieve auditees’ financial, service delivery and compliance objectives. Such assurance providers include senior auditee officials, various committees (for example, municipal public accounts, and performance and audit committees) and IAFs”.
Mpumalanga	“IAFs should advise municipalities on the internal controls that can be implemented to strengthen the control environment and ensure credible reports. IAFs must continuously audit the performance measures of the municipality and report to the municipal manager and performance audit committee. The Department of Finance and CoGTA in the province should capacitate IAFs to ensure that they understand the framework and regulations governing performance reporting. IAFs should include the audit of performance information in their annual plan and recommend improvements to management. IAFs should play a more effective role in tracking the progress made by municipalities in implementing management commitments in respect of previously raised audit findings”.
North West	“The IAFs should have the required capacity to consider all of the key areas required for all auditees in their portfolio (for shared services). The IAFs should make sure that their internal audit plans are aligned to the risks identified at their municipalities and should specifically focus on those key

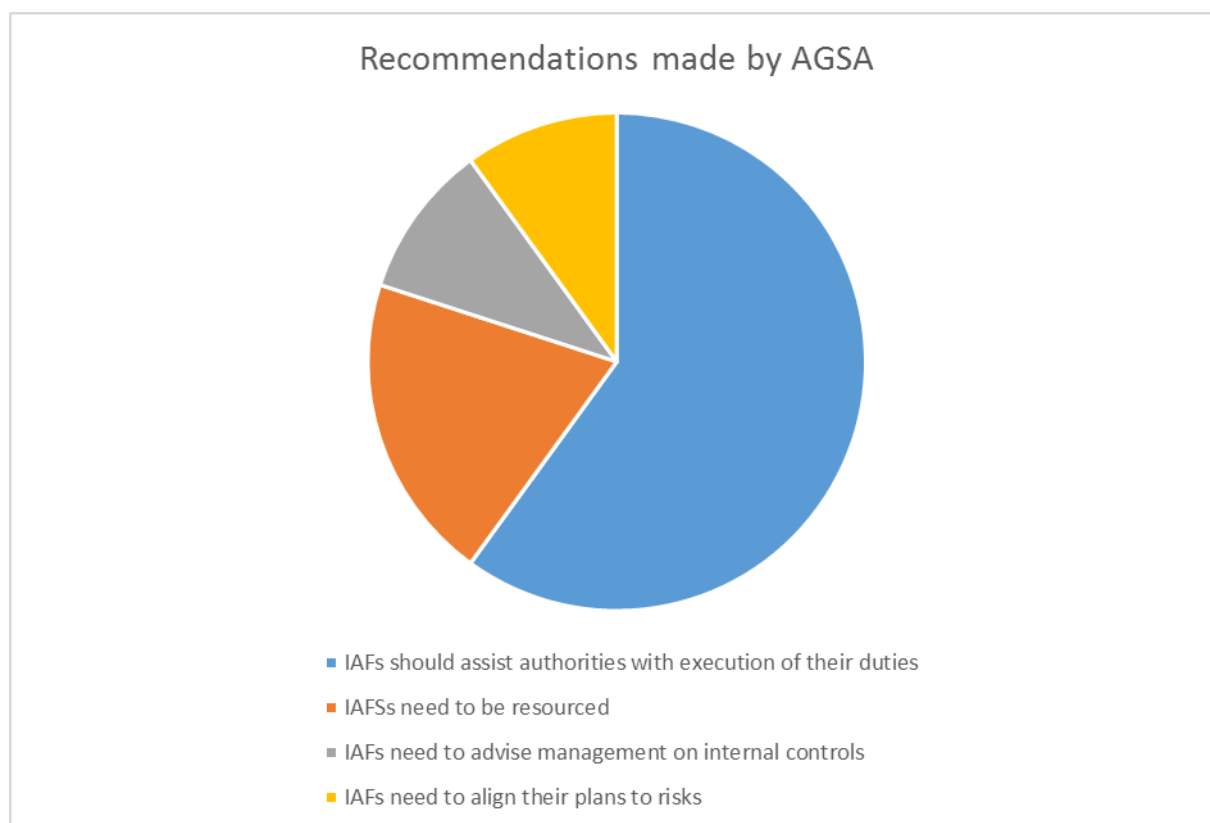
	controls directly impacting on the credibility and accuracy of financial and performance reporting and compliance with laws and legislation regulations. The unit is only effective in terms of the position it holds within a municipality, the level it reports to and the impact its resolutions have on management”.
Northern Cape	“IAFs should assist municipal managers in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation”.
Western Cape	“IAFs should assist municipal managers in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation”.

Source: AGSA reports

Based on Table 6.15 above, the key recommendations provided by AGSA to municipalities regarding their IAFs were provided. The AGSA recommended among others that the IAFs within municipalities should consider:

Assisting their accounting officers and authorities in the performance of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation. This recommendation emphasises the point that the IAFs need to be independent for them to assist and add value to their municipalities and those in authority. This recommendation is based on independency, which is one of the basic principles of internal audit. Figure 6.9 below provides an overall picture of the recommendations made by the AGSA with regard to IAFs in municipalities in South Africa.

Figure 6.9: Recommendations by AGSA in 2012/2013



Source: own research

Figure 6.9 shows that of all recommendations made by the AGSA, the recommendation stating that the IAFs should assist those in authority, such as mayors and municipal officers, in doing their daily work. The Figure clearly indicates that this recommendation has been made by the AGSA to many municipalities across the provinces of South Africa. Table 6.15 below shows the key recommendations made by the AGSA in 2013/2014.

Table 6.16: Key recommendations made by the AGSA in 2013/2014

Province	Financial year: 2013/2014
Eastern Cape	<p>“IAFs and audit committees need to ensure that all their activities are coordinated and contribute to the credibility of information”.</p> <p>“Audit committees and IAFs should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible. In addition, these committees together with council should exercise in-year oversight of performance to ensure that money is used for its intended purpose and that the anticipated return on investment is achieved. Audit committees and IAFs should assist by identifying breaches of legislation and reporting breaches to the</p>

	leadership for action to be taken against those responsible. Municipalities should ensure that an adequately resourced and functioning internal audit unit and audit committee are in place and that their reports are responded to.”
Free State	“Audit committees and IAFs should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible. In addition, these committees, together with council, should exercise in year oversight of performance to ensure that money is used for its intended purpose and that the anticipated return on investment is achieved. Audit committees and IAFs should assist by identifying breaches of legislation and reporting these breaches to the leadership for action to be taken against those responsible. Ensure that recommendations from IAFs and audit committees are developed into actions plans that are adequately implemented and monitored to ensure improved outcomes”.
Gauteng	“The administrative leadership, through IAFs, should review the business processes and operational plans to ensure an improvement in daily operations and service delivery”.
Kwazulu-Natal	“IAFs, audit committees should ensure a more coordinated effort to address identified risks relating to financial and performance management and compliance with legislation. Value-adding reviews should be conducted by IAFs and audit committees on performance information and the processes of preparing performance reports”.
Limpopo	“IAFs and audit committees should be guided to focus on the key internal control challenges faced by auditees in order to provide the leadership with focused and timely feedback on the sustainable addressing of these shortcomings”. “Management should ensure that recommendations from IAFs and audit committees are developed into action plans, which are adequately implemented and monitored to ensure improved outcomes. A well-functioning internal audit unit can play a critical role in ensuring the credibility of financial and non-financial information used for decision-making purposes. Senior management, municipal managers and mayors should take advantage of the services that IAFs can provide in this regard”.
Mpumalanga	“The implementation of the recommendations of various role players, including those of IAFs, audit committees, members of the mayoral committees, MPACs and councils, should be tracked and monitored monthly”.
North West	“Municipal Public Accounts Committees (MPACs), audit committees and IAFs should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible. In addition, these committees, together with the councils, should exercise in-year oversight of performance to ensure that money is used for its intended purpose and that the anticipated return on

	investment is achieved”.
Northern Cape	“Audit committees and IAFs should assist by proactively identifying breaches of legislation and reporting the breaches to the leadership for action to be taken against those responsible. The IAFs and audit committees should focus on the delivery of their mandate in terms of the MFMA”.
	“Municipal public accounts committees, audit committees and IAFs should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible”.

Source: AGSA reports

Based on the Table 6.16, the following analysis and summary is illustrated in Figure 6.17 below, to show the most important recommendations made by AGSA in 2013/2014 financial year in municipalities. The IAFs are expected to do the following:

- Assist their councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible.
- Exercise an oversight role to ensure that their municipalities’ resources are used for their intended purpose, and that the anticipated return on investment is always achieved.
- Assist their municipalities and those in authority by identifying breaches of legislation and reporting such breaches to those in authority for action to be taken against those responsible.
- Assist those in authority in reviewing the business processes and operational plans to ensure that an improvement in daily operations and service delivery is achieved.
- Provide more coordinated efforts to address identified risks relating to financial and performance management and compliance with legislation.
- Be guided to focus on the key internal control challenges faced by their municipalities in order to provide leadership and timely feedback on sustainably addressing these shortcomings.
- Assist in monitoring and tracking the implementation of the recommendations made.

Table 6.17: Key recommendations made by the AGSA in 2014/2015

Province	Financial year: 2014/2015
Eastern Cape	“The IAFs assist municipal managers and the CEOs of municipal entities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation. The establishment of IAFs is a requirement of legislation. An effective internal audit unit should be well-resourced to help

	<p>in improving internal controls and have a positive impact on audit outcomes”.</p> <p>“Council, municipal managers and senior managers should implement the recommendations of IAFs and audit committees and use the opportunity to interact with these bodies to assist in improving governance and control. Areas where these governance structures can jointly make significant contributions to the audit outcomes include the following”:</p> <p>“Encourage senior management to submit regular financial and performance reports for audit committee review;</p> <p>Assist with designing the audit action plan and monitor the implementation thereof; and</p> <p>Review financial statements and annual performance reports before submission for auditing to identify material misstatements”.</p>
Free State	Same as above
Gauteng	Same as above
Kwazulu-Natal	Same as above
Limpopo	Same as above
Mpumalanga	Same as above
North West	Same as above
Northern Cape	Same as above
Western Cape	Same as above

Source: atlas.ti output

Based on Table 6.17 above, the important responsibility is placed on IAFs in municipalities to ensure that the IAFs provide independent assurance on internal controls, financial information, risk management, performance management and compliance with laws and regulations. The establishment of a well-resourced IAF is also highlighted as an important quality for the functioning of IAFs because if they are well resourced, they will be able to conduct all the necessary tests, which will result in providing better services to those they serve. Table 6.18 below shows the key recommendations made by AGSA in 2015/2016.

Table 6.18: Key recommendations made by the AGSA in 2015/2016

Province	Financial year: 2015/2016
Eastern Cape	“Assist with designing the audit plans and monitor their implementation. Review the financial statements before submission for external auditing to identify material misstatements. Consider tracking the progress made in implementing management commitments in respect of previously raised IT audit findings, and improve IT controls in general”.
Free State	Same as above
Gauteng	Same as above
Kwazulu-Natal	Same as above
Limpopo	Same as above
Mpumalanga	Same as above
North West	Same as above
Northern Cape	Same as above
Western Cape	Same as above

Source: AGSA reports

Based on Table 6.18 above, it is clear that while the performance of the IAFs in municipalities has improved significantly from previous financial years, the AGSA has still made recommendations that are similar to those made previously, except for the recommendation on IT audit findings that the IAFs need to look into in their audits as well. It can be deduced from the findings and recommendations of the AGSA that similar areas of concern are provided almost every financial year, indicating that the IAFs are making slow progress towards the point where the AGSA expects them to be. Therefore, it is clear that a practical framework is indeed required to assist these IAFs to add the expected value.

6.2.8 Challenges preventing smooth-running of the IAFs

Objective of the study analysis

To provide text on the views of the AGSA regarding the key challenges preventing the smooth-functioning of IAFs in South African municipalities.

The findings

Analysis of the AGSA audit reports for the financial years 2011/2012 to 2015/2016 indicated that the following were the main challenges raised regarding the smooth running of IAFs in municipalities, as shown in Table 6.19 below.

Table: 6.19: Challenges preventing smooth running of IAFs

“Audit committees and IAFs should be fully compliant with the laws and regulations governing them, as part of the execution of their mandate. The audit outcomes reflect that 14% of the audit committees, and 6% of the IAFs, were not fully compliant. The instances described below have relevance, as the audit committees did not meet at least four times per year, the effectiveness of IAFs was not reviewed, and risk-based plans were not in place for the internal audit unit. Internal audits are not conducted in compliance with the Internal Audit Standards, and were not fully resourced by staff and technology.

Internal audit plans were found to be incomplete in some municipalities. Action taken by the IAFs was not strong with regard to independence and objectivity.

Capacity constraints and limited budgets further affected the ability of the IAFs to conduct their audits in a manner codified by the Institute of Internal Auditors.

Findings on procurement processes and contract management indicated an environment where the leadership and oversight bodies, such as the IAFs, gave insufficient attention to the implementation, enablement, enforcement, and monitoring of compliance to SCM legislation. Municipalities and municipal entities that continue to incur irregular expenditure suffer from poor internal control culture, with inadequate emphasis on the prevention and detection of deviation from SCM prescripts.

The audit committees and the IAFs were also restricted in carrying out their oversight responsibility as independent advisory bodies to the council, due to their not being taken seriously by the leadership; their recommendations being not addressed timeously; poorly capacitated IAFs; and poor quality of information submitted. IAFs did not provide enough assurance in the

areas that the legislation requires them to audit and report on.

Some expenditure was not investigated, as the oversight bodies such as the IAFs of municipalities did not have sufficient knowledge of the legislation.

There should be robust oversight of reporting on predetermined objectives by internal audit and audit committees. The oversight bodies, such as the IAFs, were to a large extent neglecting their oversight responsibilities. The competencies and skills of oversight members were not adequately assessed, resulting in oversight structures being unable to fulfil their oversight roles adequately”.

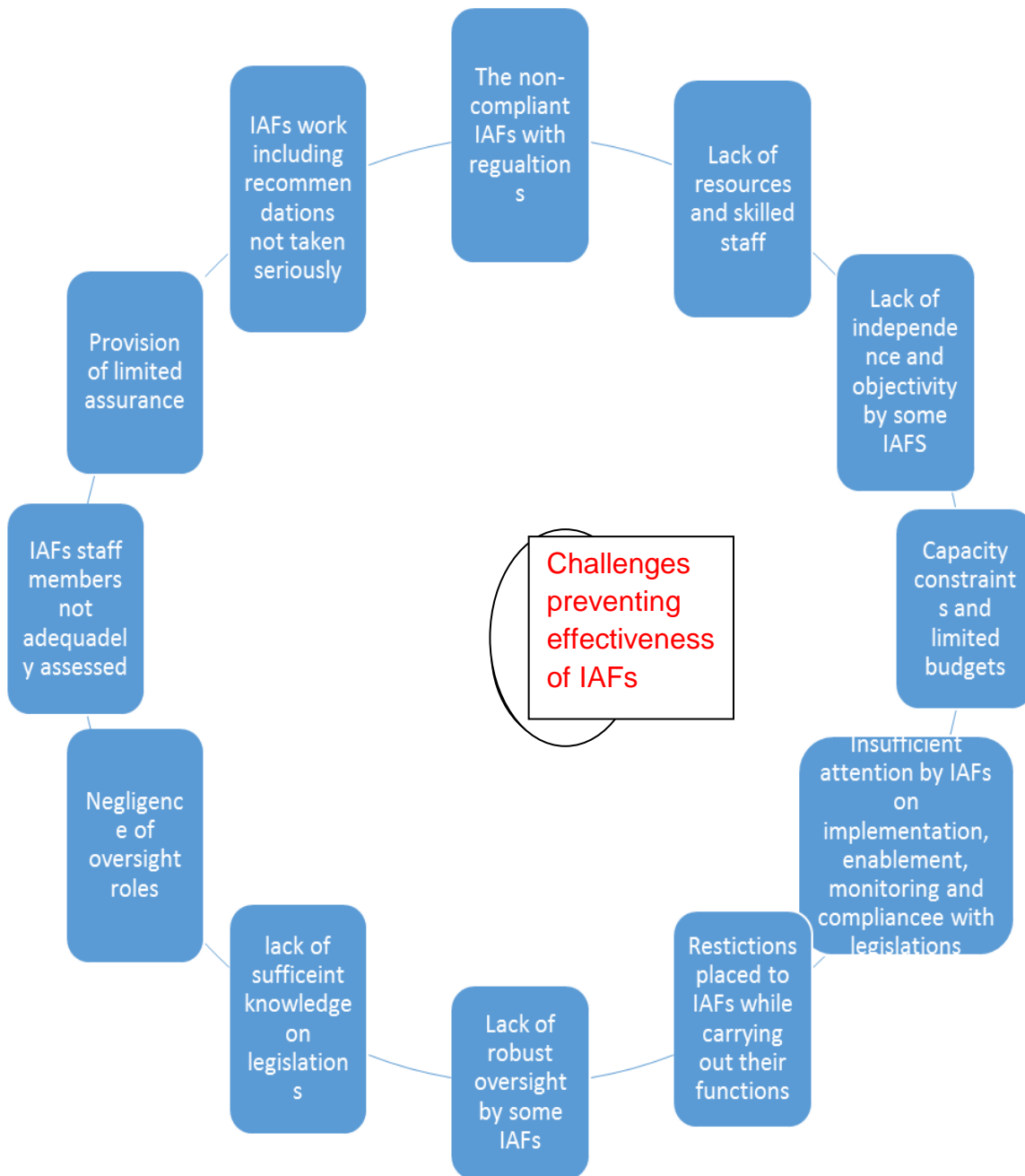
Source: AGSA reports

Based on Table 6.19 above, the following challenges were deduced, which prevented the smooth running of IAFs in South African municipalities:

- The IAFs are not fully compliant regarding the regulations stated in the MFMA.
- The IAFs are not fully resourced and lack skilled staff.
- Lack of proper independence and objectivity by some IAFs when conducting their functions.
- Capacity constraints and limited budgets affect the ability of IAFs to conduct their audits in a manner codified by the Institute of Internal Auditors.
- Insufficient attention placed by IAFs in implementation, enablement, enforcement and monitoring of compliance with legislation.
- IAFs and audit committees being restricted in carrying out their oversight responsibilities as independent advisory bodies.
- IAFs not taken seriously by their municipalities. Their recommendations not being addressed.
- Provision of very limited assurance by IAFs in the areas required by legislation.
- Lack of sufficient knowledge on legislation by some IAFs and their staff members.
- Lack of robust oversight of reporting on predetermined objectives by IAFs.
- Negligence of oversight role by some IAFs.
- IAF staff members not adequately assessed in terms of skills and competencies to perform the internal audit work.
- Lack of training by IAF staff members

These challenges are summarised in Figure 6.10 below.

Figure 6.10: Challenges preventing the effectiveness of IAFs



Source: own research

Based on Figure 6.10, the following analysis can be made:

Non-compliance of the IAFs

The IAFs are not fully compliant with the regulations as stated in the MFMA. Various legislation guides the establishment and functioning of IAFs in municipalities, however, it has been raised in the AGSA reports that such legislation is not fully followed by the IAFs, hence their non-compliance.

Lack of resources and skilled staff

The IIA through its standards (standard 1100) requires IAFs, irrespective of their size, to ensure that they are fully resourced to enable them to carry out all required responsibilities, and where resources are not sufficient, the relevant level of management should be informed. In the case of municipalities, the IAFs should approach the audit committee and report this challenge. The IIA standards further require that the IAFs and their staff members need to be skilled in all areas of audit to perform their work with the necessary competency, which is not the case in municipalities, as indicated above. Therefore, IAFs need to take this challenge seriously and ensure that it is brought to the attention of their senior management in order to obtain resources and skilled staff who will assist both the IAFs and the municipalities in providing quality work.

Lack of independence and objectivity by some IAFs

As indicated in this study and in literature reviewed, the IAFs independence forms the cornerstone of every IAF. The IIA standards require IAFs to be independent from the management and the municipality. It is therefore recommended that all IAFs should perform self-introspection on the issues of independence and objectivity, to ensure that the work they render to their municipalities will be trusted by those in authority. This can be achieved by reading the mandate to ascertain what must be investigated or audited, and at which level the findings are presented.

Capacity constraints and limited budgets

IAFs are expected to conduct their audits in all spheres of municipalities; therefore, they should be capacitated and provided with the necessary budgets to enable them to perform all the functions required. This is possible if the management of the IAFs can provide management with the budget well in advance, to ensure that it will be provided. It should be noted that the quality of the work produced can also cause IAF budgets to be lowered. IAFs must perform their functions in accordance with the IIA standards, and attain the required quality.

Insufficient attention placed by IAFs on implementation, enablement, enforcement, and monitoring of compliance with legislation

While performing their functions, IAFs are expected to pay necessary attention to the following: implementation of recommendations made by IAFs, enablement, enforcement, and monitoring of compliance with legislation. It is therefore important for IAFs to ensure that that municipalities pay thorough attention to the implementation of recommendations, by ensuring that necessary follow-up audits and enquiries are performed on regular basis. Tracking of documents needs to be

developed to deal with this aspect. In many respects, IAFs are considered to be champions of regulation, and should be able to monitor the level of compliance within their municipalities. This ensures that they add the required value.

Restrictions in carrying oversight responsibilities

The IAFs should strive for a good relationship with the highest level of management. Once such a relationship is established and maintained, it is possible for IAFs to report any frustrations experienced while performing their functions. IIA standards require that internal audits should be conducted free from any restrictions in order to provide objective and unbiased results. If this is not provided, the highest management level should be informed to produce the necessary remedies.

IAFs' work not taken seriously

As depicted in Table 6.17, a number of the findings in municipalities indicated that the work of IAFs, including their recommendations, was not being taken seriously. Reasons for this attitude should be thoroughly investigated by the IAF management. This is important, as municipalities might have genuine reasons for this behaviour, such as: cases where the IAFs have not pointed out challenges to be faced, or IAFs providing findings or risks that are very low in terms of impact etc. Therefore, the IAFs should continuously determine whether they are still relevant in their reporting, and are adding the required value, which can be done through interviews with senior management of the municipalities, or by running periodic surveys.

Provision of limited assurance

As stated above, IAFs are expected to continuously determine whether they provide the relevant value to their municipalities, and must provide assurance within the municipality on how operations function. Using up-to-date practices can assist management in achievement of their goals and stated objectives.

Lack of sufficient knowledge on legislations

IAFs are expected to be experts in a range of areas, including having sufficient knowledge of the legislation that needs to be followed by their municipalities in their operations. Therefore, IAFs should continuously ensure that their staff members are well equipped with knowledge on the legislation that governs municipalities. This assists staff members to timeously advise management

when deviating from a particular legislation. Therefore, regular workshops, attendance of professional bodies' seminars, and compliance with relevant continuous professional development (CPD) can assist.

Lack of robust oversight

It is important for IAFs to perform a vigorous and robust oversight, which is achieved when all areas of operations within municipalities are audited, and those in authority are continuously engaged in their work, plans and targets. Engaging with senior management at the highest level concerning any finding by the IAF must take place without any apprehension,

Negligence of oversight roles by some IAFs

It is unfortunate to note that some IAFs neglect their own oversight roles within their municipalities and are becoming or seen to be becoming part of the municipality. It is important for IAFs to realise that while they are a part of municipalities in terms of being employees, they should be fully independent while performing their functions. And for the IAFs to be effective, they need to continuously consult their charter and determine on regular basis as whether they still performing their functions as per this charter.

Lack of assessment of IAF staff

It is important for any employee of any organisation to be assessed on the work he/she is doing. The staff members of IAFs need to be continuously assessed to confirm that they are still performing their internal audit work properly and that they still fit. This can be done through performance appraisals, as recommended by the IIA standards. IAFs should also adopt quality reviews, in which their IAFs are evaluated regularly by external reviewers on whether they still perform their work diligently and are providing quality work.

This finding addresses one of the theoretical objectives of this study that states that: to identify challenges that prevent the smooth functioning of the IAF in South African municipalities.

6.3 SUGGESTED FRAMEWORK FOR EFFECTIVE IAFs

Based on the findings and results obtained in this chapter, here are specific characteristics that should be present for any IAF to perform optimally and add the required value within their municipality. As discussed above, these characteristics are:

Resourced and skilled competent staff who will be able to:

- Assist those in authority to make informed decisions
- Assist those in authority to execute their duties
- Provide timely and credible reports
- Assist in risks identification and make practicable recommendations
- Assist in reviewing business processes and operational plans
- Advise those in authority on internal controls
- Assist the AGSA to rely on their work
- Assist in identifying breaches of legislation

On the other hand, IAFs needs to be independent at all times to provide the required value within their municipality. The following formula interprets the meaning of IAF independence:

Reliable and sustainable outcomes = Independent IAF + quality reports + credible reports.

There are important responsibilities that IAFs within municipalities should always fulfil to add value and justify their existence. These responsibilities were fully discussed above in 6.1.2 as:

- Be properly resourced and skilled, and produce timely, relevant, and quality reports on the systems of internal control within their municipalities.
- Should define their roles and responsibilities clearly, and hold transgressors accountable.
- Should identify the gaps within their internal audit process which limit the amount of reliance that the AGSA can place on their work for external audit purposes, and the role of the IAF around performance information.
- The IAFs should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible.
- The IAFs should assist accounting officers and management in the performance of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.
- The IAFs of both the districts and local municipalities should be sufficiently capacitated with skills to assist with actively following up on information technology commitments.

- The IAFs and audit committees should provide credible reports.
- The IAFs should make sure that their internal audit plans are aligned to the risks identified in their municipalities, and should specifically focus on those key controls that directly impact on the credibility and accuracy of financial and performance reporting and compliance with laws and the legislated regulations.
- The ACs and IAFs should assist in identifying gaps of legislation, and reporting these breaches to the leadership for action to be taken against those responsible.
- The IAFs should review the business processes and operational plans to ensure an improvement in daily operations and service delivery.
- A well-functioning IAF can play a critical role in ensuring the credibility of financial and non-financial information used for decision-making purposes.
- The IAFs should advise their municipalities on the internal controls that can be implemented to strengthen the control environment and ensure credible reports.
- The IAFs should play a more effective role in tracking progress made by municipalities in implementing management commitments in respect of previously raised audit findings.
- The IAFs should identify risks and the controls to be implemented to mitigate the risks.

There are important roles that the IAFs within municipalities should fulfil to add value and justify their existence. These roles were fully discussed above in 6.1.3 above as:

The oversight role was found to be the dominant role of IAFs in all the municipalities. All other roles as recommended by IIA standards and in the literature, such as deterrence, foresight, insight and detection roles were found to be less emphasised and in most cases, not mentioned.

Training was identified as one of the pillars that municipalities can use in ensuring that all the municipal personnel including internal auditors understand their environment. Training was identified as an on-going process that can assist IAFs staff members to understand their work and perform better in their audit functions. Based on the AGSA reports analysed, it was clear that majority of the staff personnel lacks the necessary training that can assist them in performing their duties resulting in errors being done. Both the literature and the AGSA reports analysed suggest that training of IAFs staff members can result in real-time audit assessments and efficiency of the IAFs which can lead to an effective IAF. Therefore, the developed framework places training as one of the most important elements of an effective IAF, of which if regularly provided to IAF staff members and all other staff members the municipalities can be efficient and able to deliver on their mandate.

The annual or regular reviews of the IAFs' work is identified as important and crucial for the effectiveness of an internal audit as this will determine as whether IAFs add any value to their municipalities or not. The literature together with IIA standards (standard 2000) suggest and require that every IAF should be reviewed at least once annually. This reviews assist the IAF to reflect and introspect themselves on the work they provide to their organisations. Therefore, the developed framework in this study suggests that all the IAFs in the municipalities in South Africa need to conduct regular reviews both internal and external reviews to ensure that quality work is provided to municipalities at all times.

Key findings specifically raised by the AGSA regarding IAFs, were identified as:

Although IAFs were established in many municipalities, they did not contribute positively to the audit outcomes received by those municipalities, meaning that the IAFs were not adding the expected value, and were therefore redundant. This finding was raised in all provinces, as indicated in Tables 6.8 – 6.11, and dominated the findings raised by the AGSA, which highlighted that the root cause was lack of sufficient resources and competent skilled internal auditors, who could have assisted the IAFs in performing their functions optimally.

Recommendations made by the AGSA in 2011/2012 to 2015/2016, clearly showed that for the IAF to function properly, the following need to occur:

- IAFs should assist their councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible.
- IAFs should exercise an oversight role to ensure that their municipalities' resources are used for their intended purpose, and that the anticipated return on investment is always achieved.
- IAFs should assist their municipalities and those in authority by identifying breaches of legislation and report such breaches to those in authority for action to be taken against those responsible.
- IAFs should assist those in authority in reviewing business processes and operational plans to ensure that an improvement in daily operations and service delivery is achieved.
- IAFs should provide more coordinated effort to address identified risks relating to financial and performance management and compliance with legislation.
- IAFs should be guided to focus on the key internal control challenges faced by their municipalities in order to provide the leadership with focused and timely feedback on how to sustainably address these shortcomings.

- IAFs should assist in monitoring and tracking the implementation of recommendations made.

Therefore, the developed framework suggests that all the fundamental roles of an internal auditor namely, oversight role, detection role, deterrence role and insight role should be rendered by all the IAFs to ensure that the IAFs add the expected value and are considered to be effective.

Internal audit charter was discussed in section 2.8 of chapter 2 above, as a management-approved document that states the purpose of an IAF, its authority, and responsibility (Van der Nest, 2016: 149). This document was described as the foundation of the independence, operations, and communication lines of internal auditing. However, it was noted no evidence exists in municipalities that this important document exists to explain all the contents discussed in section 2.8 above. This developed framework, therefore, suggests that all the IAFs need to develop this document and ensure that they get the buy-in from those in authority as it will detail to the IAF members and the senior management of what the IAF does and the powers the IAF needs in the municipality.

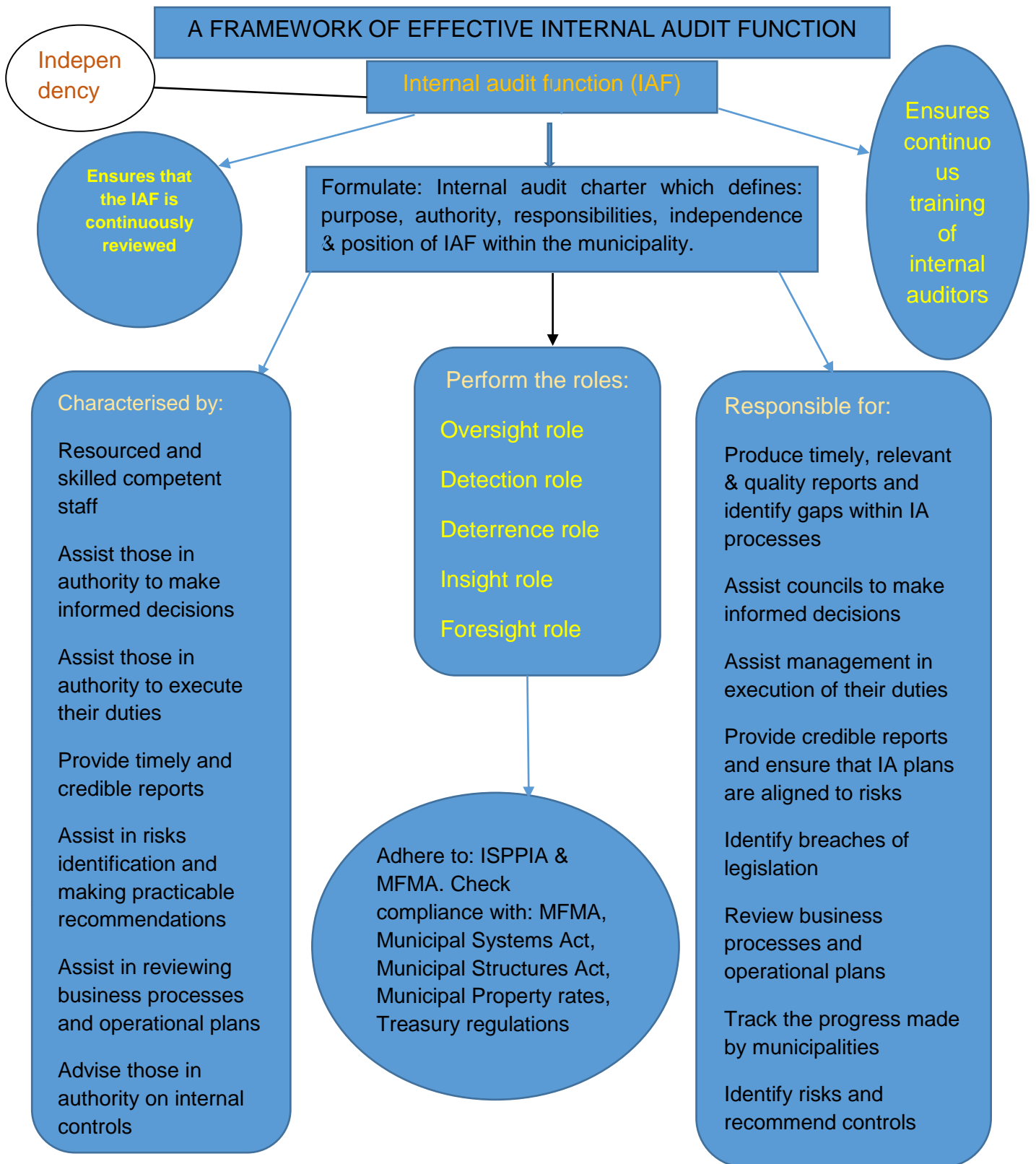
The main challenges preventing the IAFs from being effective were identified as:

- Non-compliance of the IAFs with regulations
- Lack of skills and skilled staff.
- Lack of independence and objectivity by some IAFs
- Capacity constraints and limited budgets
- Insufficient attention placed by IAFs on implementation, enablement, enforcement and monitoring of compliance with legislation.
- Restrictions in carrying out the oversight responsibilities
- IAFs not taken seriously by their municipalities.
- Provision of very limited assurance by IAFs.
- Lack of sufficient knowledge on the legislation by some IAFs and their staff members.
- Lack of robust oversight when reporting on predetermined objectives by IAFs.
- Negligence of oversight role by some IAFs.
- Lack of staff assessment.

It should be noted that a number of frameworks have been produced and developed in the past by the IIA, the Chartered Institute of Internal Auditors, and as was seen in the literature, by others such as Crowe Horwath's New Internal Audit Framework, However, all these frameworks focused on IAFs in general and not specifically those in municipalities. Therefore, those frameworks did not provide the components necessary for effective IAFs in municipalities in South Africa.

Therefore, based on all the findings, interpreted results and deductions, it can be concluded that for an IAF within a municipality to be effective, to function properly and in accordance with the IIA and the AGSA standards, the following framework presented in Figure 6.11 should be followed:

Figure 6.11: A FRAMEWORK FOR AN EFFECTIVE INTERNAL AUDIT FUNCTION



Source: own research

Based on this developed framework this formula can be derived: Internal audit charter + regular review of IAF + continuous training + independence of IAF + adherence to legislations + clear roles and responsibilities = effective IAF of a municipality in South Africa. The meaning of each variable on the framework has been explained and discussed above.

To ensure an effective IAF, senior municipal management must be trained to understand the importance of the IAFs take them seriously. Supervision of the IAFs must be performed by a well-trained official and managed by a properly functioning audit committee.

6.4 CONCLUSION

The AGSA reports from the 2011/2012 to 2015/2016 financial years were analysed through the use of atlas.ti. These reports were analysed concentrating on the characteristics and independence of IAFs, the key findings and recommendations of the study, and the challenges preventing IAFs from running smoothly. All the necessary data in the AGSA reports was then collected, and deductions were made. These were then used in analysing, interpreting, summarising and analysing the meaning of the information to study. All the areas of interest found and analysed were taken up as a result of the objectives of this study, as contained in Chapter one.

From all the findings, deductions and analyses made, it was evident that there are specific characteristics that every IAF needs to possess to be effective. It was also found that the IAFs need to be independent to provide quality and credible reports. It was noted that there are specific roles and responsibilities required of and expected from a functioning IAF, and that in South Africa, the oversight role is considered to be the main role over all other roles. The findings also revealed the AGSA key recommendations for IAFs. All these features found, deduced and analysed, contributed to the development of the framework depicted in Figure 6.11 above which, if properly followed, the framework will empower and assist the IAFs in South African municipalities to function effectively and add the expected value.

CHAPTER 7

CONCLUSION AND RECOMMENDATIONS

7.1 INTRODUCTION

This chapter presents an overview of the study research, recommendations based on the key findings, and areas for further research. The chapter concludes this study by describing how the stated objectives in Chapter one were achieved, and how the underlying research problem was addressed. The recommendations formulated were based on areas covered by the study and on future areas of research, as indicated. The chapter further discusses the framework developed and how this framework can be implemented.

The study examined the effectiveness of IAFs in South African municipalities. A literature review was conducted, in which various sources were studied to understand the value an IAF should add to an organisation, including the municipalities. The literature review discussed the origin and nature of the IAF, its value-adding role, the rules and regulations governing the functioning of the IAFs, and what constitutes an effective IAF. This was done in Chapters 2, 3 and 4. The empirical research in this study was conducted through the use of secondary data obtained from analysis of the AGSA audit reports, as from 2011/2012 to 2015/2016. A content analysis method was used to analyse these AGSA reports, and the findings of this analysis was important in solving the problem statement stated in Chapter 1. The content analysis revealed the results, which were reported in Chapter 6. Through the results obtained, a practical framework for an effective IAF in municipalities in South Africa was developed, as presented in Chapter 6. This framework was the primary objective of the study and this objective was met.

7.2 OVERVIEW OF RESEARCH

The research problem of this study was defined as follows:

Regulation by the Municipal Finance Management Act (MFMA) regarding IAFs, states that IAFs should prepare risk-based audit plans and internal audit programmes for each financial year, and advise the accounting officers accordingly. A further report was made to audit committees on the implementation of the internal audit plan, and matters relating to internal audits; internal controls; accounting procedures and practices; risk and risk management; performance management; loss control; and compliance with this Act (MFMA), (MFMA, s165). The AGSA continues to express concern about the quality of financial governance, as evidenced by the adverse audit opinions issued annually by the AGSA (Auditor-General South Africa, 2014: 34, 39, 79, 109; Auditor-General South Africa, 2013: 31, 35, 75, 103; Auditor-General South Africa, 2012: 86; Auditor-

General South Africa, 2011: 32). The AGSA specifically states that IAFs in municipalities do not adequately evaluate internal controls, and therefore do not fully advise or report to the audit committees on these matters (Auditor-General South Africa, 2011: 32; Auditor-General South Africa, 2012: 86; Auditor-General South Africa, 2013: 31, 35, 75, 103).

According to the MFMA and the IIA, IAFs should assist in advising accounting officers, among others, on points such as internal controls, accounting procedures that will improve financial performance and practices, risk areas and management of such risks, performance management, and compliance with the appropriate laws. It is therefore evident that the IAFs in municipalities are not effective, as these municipalities continue to receive qualified disclaimers and adverse opinions from the AGSA on yearly basis. The problem is that no specific framework is in place to guide the IAFs on how to function and assist in this sphere of government, to ensure that they remain effective and add value to their organisations while remaining independent, as required by the legislation.

In order to address the research problem, specific focus areas were formulated and addressed extensively through the literature review and empirical work. The AGSA reports for sampled municipalities in all categories in South Africa were analysed using the Atlas.ti software to achieve the objectives of this study and to address the research problem.

The following sections provide a summary of how each objective of the study was achieved. Conclusions are presented by reviewing the main findings from the literature review and the empirical results.

7.2.1 Origin, history, nature, and development of internal auditing

In Chapter 2, the origin, history and development of internal auditing as a discipline was discussed. It emerged that the history of internal auditing started as early as 1941, and developed over time until today, when this discipline is now recognised and considered to be important in the functioning of any organisation. It was further discussed that the internal audit discipline as an important function started to emerge strongly within the public sector in the nineties, when legislation was developed to recognise the profession and encourage government entities to start practicing internal auditing.

In conclusion, internal auditing as a profession was highly enhanced by the introduction of standards, which provided guidance on how this discipline should be practiced by both organisations and practitioners. It is important that the internal auditors regardless of the sector in which they work, understand the evolution of this profession to be able to contribute to its development in the future.

7.2.2 Characteristics of an ideal IAF

In chapter 6, it was revealed that a functional IAF is one that is resourced and possess skilled competent staff, assists those in authority to make informed decisions and execute their duties; provides timely and credible reports; assist in risks identification and makes practicable recommendations; assists in identifying breaches of legislation and reviews business processes and operational plans; advise those in authority on internal controls and tracking progress made; and assists the external auditors to become reliant on the work of the IAF.

In conclusion, based on the discussions in Table 6.4, it is evident that the ideal IAF should possess a number of characteristics that, if properly practised, will add value to their municipalities. These characteristics are in line with the characteristics of the IAF as suggested by the Institute of Internal Auditors. It is further recommended that when the internal audit charters are drawn within the IAFs, these characteristics be considered to ensure that the purpose and powers of the IAF is well documented and approved.

7.2.3 The roles and responsibilities of the IAF

In chapter 2, it was discussed that a functioning IAF should provide relevant and timely reports of good quality. This means that reports produced by IAFs should be credible and be given in on time to assist the municipalities and those in authority to address he challenges and problems timeously before a major impact is experienced.

The IAFs should further assist municipalities in providing credibility in financial and non-financial information. This will assist the municipalities to submit the financial statements and other non-financial information such as statistics that are of quality and which comply with specific requirements such as GRAP etc.

The IAFs should assist municipal councils in making informed decisions. This is important for every municipality and its management as part of their mandate is to deliver services to their citizens and always act in their best interests. The functioning IAFs should assist in this regard by continuously investigating best practices on behalf of the municipalities, and advise them appropriately.

A functioning IAF should assist accounting officers to execute their duties. The MFMA requires that IAFs should be established to assist the accounting officers to perform their duties. This is possible only if the IAF are staffed by skilled and competent personnel.

A functioning IAF should ensure that its municipality is in compliance with the laws and regulations that govern the running of municipalities and its activities, such as the MFMA, Treasury regulations etc. It is the responsibility of every IAF to fully study and become knowledgeable on all regulations that need to be followed by municipalities, to fully comply with the law. The IAFs should further assist their municipalities in identifying breaches in legislation, if any, and report them timeously to the municipality's management for correction.

A properly functioning IAF should ensure that that internal audit plans are aligned to their municipalities' risks. This is important role because the IAF exists in municipalities to serve them and those in authority by identifying the risks. Therefore, in their audit plans, the IAFs need to align their plans to those of their municipalities. The IAFs should further assist in identifying risks and corrective controls that can be implemented to mitigate such risks.

A well-functioning IAF should assist its municipality in reviewing its business processes and operational plans. Municipalities are established to provide services to the people residing within them. They do so by providing various services such as water supply, electricity, sanitation, roads etc. It is therefore important for every IAF existing within municipalities to assist in reviewing its normal business processes and operational plans. This is done by continuously evaluating whether the operational plans and business processes are actually meeting citizens' expectations and are of best practice.

A well-functioning IAF should assist in tracking the progress made by the municipality in implementing previous findings. The findings previously raised by either the IAF or by the AGSA are important and must be addressed to ensure that there is progress in the municipality regarding areas raised, and for development of the municipality. The IAF should always track the findings that have been addressed so that challenges in those areas are not repeated.

In conclusion, a checklist that could be used by municipalities in South Africa was suggested in Figure 6.3. This checklist can be used to determine whether the IAF fulfils its roles and responsibilities as expected by the legislation and the AGSA

Therefore, the IAF should be the 'eyes and ears' of senior management, giving them honest and clear information about organisational affairs at all times. This was seen as the most important responsibility that IAFs should provide within their organisations across the board. It was further discussed that IAFs are important components of the audit committees. The following were identified as the most important roles that should be played by every IAF to be regarded as value adding and effective: oversight, detection, deterrence, insight and foresight roles.

In conclusion, it was found that all the roles indicated above play an important role in any IAF and need to be fulfilled to ensure that the IAF is seen as effective and functioning.

7.2.4 Independence of the IAF

Chapter 2 discussed that IAFs should be independent from management in order for them to be trusted and their recommendations taken seriously. This was found to be supported by the standard 1100 of the IIA on independence and objectivity, which states: “the IAF must be independent and internal auditors must be objective in performing their work”. It is therefore expected that the CAE of the IAF within a municipality must report to a level within the municipality that allows the IAF to fulfil its responsibilities. It was not clear from the AGSA reports analysed on what levels are the IAFs reporting. This can be another area of further research.

In conclusion, it was found that while IAFs within the public sector, such as in municipalities, are expected to be independent at all times, the independence of IAFs is normally threatened by some employees using the IAF as a stepping stone to other positions; Accounting officers approve the IAF's budget and provide input for the internal audit plan, and consider the internal auditor to be a “partner”, especially when dealing with indirect threats, which place a major risk on the independence of IAFs and their functioning.

7.2.5 Rules and regulations governing internal auditing

In Chapter 3, the rules and regulations governing IAFs in South Africa’s local governments were discussed as follows:

The International Standards for the Professional Practice of Internal Auditing (Standards) are compulsory requirements for the professional practice of internal auditing and for evaluating the effectiveness of its performance. These standards are expected to be applied in all environments in which the IAF is in place.

The MFMA Act (2013), is aimed at ensuring that there is a complete and sustainable management of the fiscal and financial affairs of municipalities and municipal entities by establishing norms, standards, and other requirements in order to achieve the municipal objectives.

The Local Government: Municipal Systems Act 32 of 2000, was promulgated to enable municipalities in South Africa to provide social and economic support where necessary for the benefit of the residents within South African municipalities.

The Local Government: Municipal Structures Act 117 of 1998, was promulgated with the aim of providing guidance on the establishment of different types of municipalities as allowed by the

Constitution of South Africa. Among other aims, this Act aimed to provide for the establishment of municipalities in accordance with the requirements relating to categories and types of municipality.

The Local Government: Municipal Property Rates Act, 2004, which was aimed at regulating the power of a municipality to impose rates on property; exclude certain properties from rating in the national interest; make provision for municipalities to implement a transparent and fair system of exemptions, give reductions and rebates through their rating policies; make provision for fair and equitable valuation methods of properties; make provision for any objections and appeals processes, etc.

Treasury regulations are special regulations that are provided by the Minister of Finance through Section 168 (1) of the MFMA, acting in consultation with the cabinet member responsible for local government (mainly the Minister of Local Government), such as financial management and internal controls, etc.

It is evident that the environment in which municipalities exist in South Africa is controlled by a number of legislations that need to be followed. These legislations need to be well understood to ensure that they are well implemented. Municipal personnel including the IAF staff need to be well trained to be in the position to understand and implement these changes.

In conclusion, all municipalities established in South Africa, regardless of their category and size, are expected to comply with the following regulations: ISPPA, MFMA, Municipal Systems Act (2000), Municipal Structures Act (1998), Municipal Property Rates Act (2004), and all Treasury regulations.

7.2.6 The Audit committees

In Chapter 3, the MFMA (sections 165 & 166) state that audit committees' functions are considered important for every municipal council. ACs are expected to perform the responsibilities assigned to them by the MFMA (sections 165 & 166), and the corporate governance responsibilities delegated to them by their council, under its charter.

In conclusion, it was found that audit committees are expected to assist the IAFs in performing their functions within their organisations. This recommendation is important to the ACs as they rely on the value-adding and effective work of the IAFs. Therefore, the following benefits will be realised by audit committees which support their IAFs: ensuring an independent IAF which operates efficiently and effectively; ensuring that risk management practices are applied in the organisation; ensuring that sound corporate governance practices are applied; ensuring that the

system of internal controls is adequate and functioning effectively; and ensuring that fraud and corruption are dealt with effectively.

7.2.7 Effectiveness of the IAF

In Chapter 4, the effectiveness of the IAF was discussed. It emerged that among other things, the following determinants play an important role in assessing the effectiveness of IAFs within any organisation: organisational independence, support by senior management, quality of work done by the IAF, and professional proficiency of the internal auditors. The discussion further suggested that a balanced scorecard could be used as the instrument to measure work performed by the IAF.

In conclusion, it appears that it is always difficult to measure the effectiveness of any phenomenon. However, there are certain determinants and instruments that can provide clear guidance on whether the IAF is effective or not, such as those suggested in this study and its framework.

7.2.8 Challenges preventing smooth running of IAFs

In chapter 4, the challenges preventing the smooth running of IAFs were discussed as follows:

Failure to comply with the relevant legislations and regulations as promulgated, such as those of the MFMA, Treasury regulations, etc. Lack of knowledge or disregard of the legislation and processes by municipal councillors and officials; failure to appoint suitably qualified key individuals to specifically legislated tasks; and an inability or disregard by municipalities to establish and maintain the appropriate control systems which provide the basis of the governance framework. Some municipalities were found to have inadequate financial management capacity, which resulted in weak budgetary, accounting, credit control and financial reporting systems.

In conclusion, the weak leadership in strategic management, including corporate governance, has resulted in a shortage of skills to implement financial management; disregard of legislation; misplacement of skills within municipalities; politically motivated appointments of senior managers without the required qualifications; and had tremendously weakened the performance of municipalities in general.

7.3 Key findings regarding IAFs

The following section provides the key empirical findings:

7.3.1 Responsibilities of the IAF

The IAFs within municipalities are not fulfilling all their responsibilities in their performance of audit functions, leading to these municipalities obtaining qualified audit opinions, disclaimer opinions and claims of mismanagement of resources.

7.3.2 Roles of IAFs

There is a lack of adequate progress within the municipalities due to inadequate oversight by the IAFs, as they are not always fully capacitated with skilled, experienced staff to fully perform the oversight function. As suggested in the literature, emphasis is placed on the oversight role of the IAF, rather than on all other roles, such as the detection, deterrence, insight and foresight roles.

7.3.3 Independence of IAFs in municipalities

Based on the qualitative extract in Table 6.4, the IAFs in municipalities are not provided with appropriate and independent channels of reporting within the municipalities.

7.3.4 Types of opinions obtained

Based on this empirical study, it was found that municipalities obtain qualified opinions and adverse opinions, with no improvement in sight. However, it is encouraging to note a declining trend with the municipalities obtaining disclaimers, as these municipalities declined from 78 in the 2011/2012 financial year to only 32 in the 2014/2015 financial year. And the number of municipalities which obtained unqualified opinions with no findings improved from 10 municipalities in 2011/2012 to 72 municipalities in 2014/2015.

7.3.5 Key reasons for the findings

The following were key reasons provided by the AGSA regarding the qualified, disclaimer and adverse opinions provided to municipalities: non-compliance with laws and regulations; increase in irregular and unauthorised expenditure; awarding of contracts irregularly; and lack of positive impact by both the audit committees and the IAFs. All these findings were raised in the 2011/2012 financial year, and had been raised prior, but with no tangible improvement. despite the fully established IAFs in these municipalities.

7.3.6 Contribution of IAFs in municipalities

Despite the fact that IAFs have become established in many South African municipalities over the years, they have not contributed positively to their audit outcomes, meaning that they have not added the expected value, and are therefore redundant.

The leadership or those in authority in many municipalities were found to not take seriously the work of the IAFs, and as a result, the same audit opinions and findings are regularly provided by the AGSA each year.

The AGSA found that the IAFs are not producing credible financial statement reports. This means that the IAFs do not review and make corrective comments on the financial statements prepared by the municipalities' management.

The IAFs were found not sufficiently addressing significant risk areas, and planned audits were not performed due to cash flow challenges in some municipalities.

7.3.7 Regulation compliance of IAFs

This study revealed that the IAFs did not comply with the following important areas outlined in the MFMA, resulting in: inadequate evaluation/advice or reporting on internal controls; poor accounting; poor risk and loss control; no reporting to audit committee on compliance with legislation; performance measurements not audited on a continuous basis; lack of quarterly reports detailing performance against annual internal audit plan, and three-year strategic internal audit plan not submitted to the audit committee.

7.3.8 Training of IAF personnel

It was revealed that the staff of IAFs in municipalities are not properly trained and lack the necessary competencies to perform their functions as required and expected. Personnel who do not have the required competencies are appointed to key positions in municipalities, and current employees do not keep up with the changing local government environment through on-going training and development.

7.3.9 IAF challenges regarding performance

The main causes for the lack of effectiveness of IAFs within municipalities were found to be:

- IAFs are not fully compliant regarding MFMA regulations;
- IAFs are not fully resourced and lack skilled staff;
- Lack of proper independence and objectivity by some IAFs when conducting their functions;
- Capacity constraints and limited budgets affect the ability of IAFs to conduct their audits in a manner codified by the Institute of Internal Auditors;
- Insufficient attention placed by IAFs in implementation, enablement, enforcement and monitoring of compliance with legislation;
- IAFs and audit committees being restricted in carrying out their oversight responsibilities as independent advisory bodies;
- IAFs not taken seriously by their municipalities. Their recommendations not being addressed;
- Provision of very limited assurance by IAFs in the areas required by the legislation.
- Lack of sufficient knowledge on legislations by some IAF and their staff members;
- Lack of robust oversight of reporting on predetermined objectives by IAFs;
- Negligence of some IAFs in performing oversight role; and
- IAF staff members not adequately assessed in terms of skills and competencies to perform the internal audit work.

7.4 RECOMMENDATIONS

Based on the literature review and the results of this study, the following recommendations are made:

7.4.1 To IAFs in municipalities:

Regarding IAF responsibilities:

Every IAF in municipalities should fulfil all the roles and responsibilities outlined above, irrespective of the category or size of the municipality. The municipality should use the checklist depicted in Figure 6.3 to continuously gauge whether they continue to fulfil all the necessary roles and responsibilities expected.

Regarding IAF roles:

All the IAFs should start fulfilling all roles expected of them, including: oversight, detection, deterrence, insight and foresight.

Regarding IAF independence:

The IAF should be independent, and be seen to be independent from management, in order to perform their functions freely and without any interference, thereby adding the required value.

Regarding types of opinions provided by AGSA:

All municipalities should ensure that there is a functioning audit committee that supports the functioning of internal auditing.

Regarding the IAF contribution:

All IAFs are expected to measure and assess their contribution to their municipalities' a least once a year. This should be done by external party to ensure objectivity.

The IAFs should form an integral part of the provision of assurance within their municipalities.

Regarding IAF compliance with regulations:

IAFs are regarded as an important component of oversight within any organisation that leads by example. It is expected that every IAF should comply with all the necessary regulations to ensure that it is adding the required value.

Regarding training of internal auditors within IAFs:

To ensure an effective IAF, senior municipal management must understand the importance of the IAF, and take it seriously. Further, supervision of the IAF must be performed by well-trained officials managed by a properly functioning audit committee.

Municipalities should consider collaborating with local universities and training colleges to assist them with specific skills gaps.

Regarding challenges faced by IAFs:

- IAFs should be fully compliant with the regulations as stated in the MFMA, and should lead by example as the first departments in municipalities to comply with the stated regulations.

- The CAEs of the IAF, with the help of the audit committees, should ensure the functioning of a fully resourced IAF that is adequately staffed with skilled and competent employees.
- Proper independence and objectivity should prevail in all municipal IAFs, to ensure that audit functions are conducted freely and objectively.
- All the IAFs should be fully resourced by their municipalities to ensure that they deliver reliable and quality work that is performed in a manner codified by the Institute of Internal Auditors.
- Sufficient attention should be placed by IAFs on the implementation, enablement, enforcement, and monitoring of compliance with legislation.
- The IAFs and audit committees should enjoy a free role in carrying out their oversight responsibilities as independent advisory bodies.
- IAFs should be taken seriously by their municipal management, and all their recommendations should be addressed. This would only be possible if the IAF are adequately resourced and enjoy the freedom they need to perform their functions.
- IAFs should give full assurance in the areas required by the legislation, as provided by the MFMA.
- All members of the IAF should possess sufficient knowledge and competency on the legislation to perform their daily functions. This can be obtained through regular training and compliance with CPD requirements etc.
- The IAFs should strive for and provide robust oversight and timely reporting on the municipality's predetermined objectives in order to justify their existence within municipalities.
- Every member of the IAF should be adequately assessed at least annually in terms of their skills and competencies to perform internal audit work, to ensure that they continue to have the required levels of knowledge and the necessary skills to perform their functions.

7.4.2 To audit committees:

As discussed above, the MFMA holds that audit committees are important instruments in the corporate governance of every entity, including municipalities. The focus on service delivery and accountability in the public sector has increased the emphasis on good corporate governance. Audit quality and the integrity of financial reports, as well as the quality of the systems of internal control in every municipality, necessitates independent audit committees that act as a link between management, and internal and external audits. However, based on the findings of this study, it is apparent that audit committees in some municipalities are either non-existent or not performing

their expected oversight role, thereby weakening the functioning of IAFs. It is recommended that audit committees should be established in all municipalities and all responsibilities fulfilled, as provided in the King IV Report and by the MFMA.

7.4.3 To the Department of Cooperative Governance and Traditional Affairs (COGTA):

This department oversees the activities of municipalities in South Africa. The municipalities are expected to report their operations to this department, thus making it one of the key departments to the existence of the municipalities in South Africa.

It is therefore recommended that this department assist in ensuring that all the municipalities in South Africa establish functioning audit committees to assist with the establishment of functioning IAFs. If this can be achieved, the IAFs will undoubtedly provide the required oversight, which will result in smooth running municipalities, carrying out their mandate and providing the necessary services.

It is further recommended that this department provides adequate training to all councillors so that they fully understand how municipalities should operate, this ongoing training would be of benefit to all councillors and other key municipal employees.

7.4.4 To the National Treasury:

Evidence clearly showed the various challenges that face IAFs within municipalities in South Africa, which prevent these departments from performing their required work and adding value to their municipality. In this regard, guidance statements should be formulated to assist the IAFs with regard to their independence, municipal leadership taking their work seriously, adequately resourcing the IAFs, and forming of audit committees in some municipalities, all of which would fully support the work of the IAFs.

7.4.5 To the South African Local Government Association (SALGA):

As discussed in Chapter 3, SALGA aims at establishing the following responsibilities, among others, within municipalities in South Africa: to transform local government to enable it to fulfil its developmental role, enhance the role of provincial local government associations as provincial representatives and consultative bodies in local government, and raise the profile of local government. It is evident that this organisation still has a huge amount of work ahead, as it fulfils its role of ensuring the functioning of municipalities in South Africa to produce good and expected audit outcomes, and provide sound financial management. SALGA (2015) and this study have highlighted that some of the challenges facing municipalities include challenges in financial

governance within the municipalities, the absence of capacity in established audit committees, shortage of skilled internal auditors, and absence of qualified municipal officials.

In this regard, SALGA, needs to fully perceive what it means to a qualified auditor to have the right conditions in which to perform their work diligently and independently. SALGA should, therefore, assist in creating such conditions within municipalities. This will also prevent circumstances whereby people who are not qualified to be internal auditors are opportunistically given this important function of auditing. It would be advisable for SALGA to start formulating partnerships with professional organisations, such as the Institute of Internal Auditors South Africa (IIASA), and Accounting Technicians South Africa (AAT (SA)), to assist municipal employees, including those working within the IAFs, to train and develop their auditing and financial skills in order to perform their duties with competence.

7.5 KNOWLEDGE CLAIM

All municipalities in South Africa have the constitutional mandate to provide necessary services to the citizens within their jurisdiction. These municipalities are seen as critical levels of government, and as the levels at which government services are delivered. However, it has been noted over the years that these levels or categories of government continuously obtain negative audit opinions, including qualified opinions, disclaimer opinions, and adverse opinions. These types of negative opinions are obtained despite the majority of municipalities having IAFs in place. This was the reason and motivation for doing this study on the effectiveness of IAFs in municipalities in South Africa.

This study found evidence that is in line with the study's problem statement, and revealed the reasons for IAFs failing to add value to their municipalities. The study further revealed the reasons why IAFs within some municipalities are ineffective. Figure 6.11 in Chapter 6, portrays the suggested framework of the study. In following it, IAFs will produce the expected value-added, thereby becoming effective, recognised, and valued by those in authority. Therefore, the primary objective of this study being developing a practical framework for IAFs to effectively add value to their municipalities in South Africa has been met.

Effective IAFs can play an important role in developing countries such as South Africa, as such countries are still characterised by high levels of unemployment, slow economic growth, and corruption. With the help of effective IAFs, these challenges could be timeously detected and addressed.

7.6 AREAS FOR FURTHER RESEARCH

The following areas for further research are recommended:

- It should further be investigated why municipalities in South Africa, and the AGSA, highly regard and concentrate on the oversight role of the IAF as opposed to other roles, such as detection, deterrence, insight and foresight.
- Why do IAFs within municipalities in South Africa still struggle today with the independence factor?
- To establish what measures municipalities do about negative audit opinions received from the AGSA, and what measures they take to address the areas of concern raised by the IAFs, these need to be empirically investigated.
- What practical ways could be implemented within municipalities to assist the IAFs to address all the challenges that they face?
- Extend the research to other levels of government, using the same approach adopted in this study.
- Extend the research to the private sector and compare the results with the results of this study.
- Undertake comparative studies with other countries following the same approach used in this study.

7.7 LIMITATIONS OF THE STUDY

The results of this study are geared towards municipalities in South Africa, and generalisation could be applied to all the municipalities in the three categories sampled. The scope of this study is limited to areas explained in Chapter 1, and it is acknowledged that many other aspects could have impacted on the stated research problem.

7.8 CONTRIBUTION TO EXISTING KNOWLEDGE

This study contributed to the description of the effectiveness of IAFs in South African local government, focusing on all three categories of municipality, namely: metropolitan municipalities, district municipalities and local municipalities. The findings of this study thus provide a holistic view of the effectiveness of IAFs and its value-adding role in South African municipalities. The results of this study can be used by other IAFs as a benchmark for other entities and sectors, to determine how IAFs can add value and become effective. The results of this study can be used to assist IAFs to add the required value within their municipalities and become effective. By adopting the

framework suggested in this study, the IAFs (Chapter 6, Figure 6.11) can perform the expected functions within their municipalities, and justify their existence to those in authority.

The study also contributed to the existing body of knowledge in the area of public sector auditing, by analysing the three categories of existing municipalities in South Africa. This can be used in local and global studies to compare the practice of internal auditing in public sectors.

The study identified the main roles and responsibilities of IAFs in municipalities in Chapter 4 (4.9.4) and in Chapter 6 (6.2.1.2), and further used Figure 6.2 to explain these roles and responsibilities. The challenges that prevent the smooth functioning of IAFs in municipalities in South Africa were identified in Chapter 4 (4.9.5). The study also discussed what factors need to be considered by municipalities to ensure that the IAFs are functioning independently (Chapter 6, (6.2.2); Figure 6.4 and Figure 6.5). The study further identified the characteristics of an effective IAF (6.2.3), as stated in the objectives in Chapter 1.

Lastly, this study contributed to the research design and methodology for internal auditing studies, and can be used as a benchmark for data collection. In this regard, the study used Atlas.ti software to perform qualitative coding, which was assisted in quantifying and interpreting the results.

This study thus contributes to the limited existing body of knowledge regarding the effectiveness of internal auditing within South African municipalities, and it is suggested that using the study's framework will provide guidance on how IAFs in municipalities can become effective and value-adding.

7.9 CONCLUSION

The study found that the IAFs within municipalities in South Africa are adequate in only some municipalities, and these IAFs were found not to be adding the value required and expected. This became evident when the number of negative audit opinions provided annually by the AGSA to these municipalities was considered. It was found that most of the IAFs within municipalities are not effective due to several reasons, including lack of sufficient resources, lack of training, management not taking the work of the IAFs seriously, lack of proper independence between IAFs and management, and so on. If all these identified factors are not adequately addressed, IAFs in South Africa will remain ineffective and municipalities will not be able to carry out their constitutional mandate as required and expected.

The primary objective of this study as stated in the introductory chapter, was to develop a practical framework to effectively add value to organisations by facilitating the IAFs of municipalities in South Africa. As the framework for effective IAFs was developed, this study's objective was

achieved, as indicated on Figure 6.11. The framework can be used by the IAFs of South African municipalities to add value and assist their municipalities in performing and fulfilling the requirements of their mandate.

ANNEXURES

ANNEXURE A

DEFINITIONS OF CONCEPTS

Adverse audit opinion – “means the financial statements contain material misstatements that are not confined to specific amounts, or the misstatements represent a substantial portion of the financial statements”, (AGSA, 2014).

Audit committee – is a committee of the board of directors responsible for oversight of the financial reporting process, selection of the independent auditor, and receipt of audit results both internal and external. The committee assists the board of directors fulfil its corporate governance and overseeing responsibilities in relation to an entity’s financial reporting, internal control system, risk management system and internal and external audit functions.

Disclaimer audit opinion – “the auditee provided insufficient evidence in the form of documentation on which to base an audit opinion. The lack of sufficient evidence is not confined to specific amounts, or represents a substantial portion of the information contained in the financial statements”, (AGSA, 2014).

District Municipality – “A municipality that has municipal executive and legislative authority in an area that includes more than one municipality” (Constitution of the Republic of South Africa, 1996).

Effectiveness – the subjective evaluations assigned to the IAF by management. The success rate of any IAF can only be measured against the expectations of those being served (Cohen & Sayag).

Independence – “is the freedom from conditions that threaten the ability of the IAF to carry out internal audit responsibilities in an unbiased manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the chief audit executive has direct and unrestricted access to senior management and the board” (IIA, 2016).

IAF – is the function within an organisation/municipality that provides management with information, appraisals, recommendations, and counsel regarding the activities examined and other significant issues.

Local Municipality – A municipality that shares municipal executive and legislative authority in its area with a category C municipality within whose area it falls (Constitution of South Africa, 1996).

Metropolitan municipality – A municipality that has exclusive municipal executive and legislative authority in its area (Constitution of South Africa, 1996).

MFMA – the Act No. 56 that was promulgated in July 2004 to secure sound and sustainable management of the financial affairs of municipalities and other institutions in the local sphere of government.

Municipality – “a single administrative division having corporate status and powers of self-government or jurisdiction as granted by national and state laws, to which it is subordinate. A

municipality has the right to govern, on its own initiative, the local government affairs of its community, subject to national and provincial legislation, as provided for in the Constitution”, (Constitution of South Africa, 1996).

Qualified audit opinion – “means the financial statements contain material misstatements in specific amounts, or there is insufficient evidence for auditors to conclude that specific amounts included in the financial statements are not materially misstated” (AGSA, 2014).

Unqualified audit opinion – means the financial statements are free from material misstatements (in other words, a financially unqualified audit opinion) and there are no material findings on reporting on performance objectives or non-compliance with legislation, (AGSA, 2014).

Value-adding – audit work that helps management improve their operations, rather than assignments that simply verify compliance with laws and regulations.

ANNEXURE B

MUNICIPALITIES IN SOUTH AFRICA PER PROVINCE

The following Tables give the different types of municipalities found in the different provinces of South Africa.

4 Municipalities found in the Eastern Cape:

The following are the municipalities found in the Eastern Cape Province of South Africa:

Table B1: Municipalities in the Eastern Cape

Name of the municipality	Type of the municipality
Buffalo City Metropolitan Municipality	Metropolitan/ Category A
Nelson Mandela Bay Metropolitan Municipality	Metropolitan/ Category A
Alfred Nzo District Municipality	District municipality/ Category C
Amathole District Municipality	District municipality/ Category C
Sarah Baartman District Municipality	District municipality/ Category C
Chris Hani District Municipality	District municipality/ Category C
Joe Gqabi District Municipality	District municipality/ Category C
OR Tambo District Municipality	District municipality/ Category C
Amahlathi Local Municipality	Local municipality/ Category B
Baviaans Local Municipality	Local municipality/ Category B
Blue Crane Route Local Municipality	Local municipality/ Category B
Camdeboo Local Municipality	Local municipality/ Category B
Elundini Local Municipality	Local municipality/ Category B
Emalahleni Local Municipality	Local municipality/ Category B
Engcobo Local Municipality	Local municipality/ Category B
Gariep Local Municipality	Local municipality/ Category B
Great Kei Local Municipality	Local municipality/ Category B
Ikwezi Local Municipality	Local municipality/ Category B
Ingquza Hill Local Municipality	Local municipality/ Category B

Inkwanca Local Municipality	Local municipality/ Category B
Intsika Yethu Local Municipality	Local municipality/ Category B
Inxuba Yethemba Local Municipality	Local municipality/ Category B
King Sabata Dalindyebo Local Municipality	Local municipality/ Category B
Kou-Kamma Local Municipality	Local municipality/ Category B
Kouga Local Municipality	Local municipality/ Category B
Lukhanji Local Municipality	Local municipality/ Category B
Makana Local Municipality	Local municipality/ Category B
Maletswai Local Municipality	Local municipality/ Category B
Matatiele Local Municipality	Local municipality/ Category B
Mbhashe Local Municipality	Local municipality/ Category B
Mbizana Local Municipality	Local municipality/ Category B
Mhlontlo Local Municipality	Local municipality/ Category B
Mnquma Local Municipality	Local municipality/ Category B
Ndlambe Local Municipality	Local municipality/ Category B
Ngqushwa Local Municipality	Local municipality/ Category B
Nkonkobe Local Municipality	Local municipality/ Category B
Ntabankulu Local Municipality	Local municipality/ Category B
Nxuba Local Municipality	Local municipality/ Category B
Nyandeni Local Municipality	Local municipality/ Category B
Port St Johns Local Municipality	Local municipality/ Category B
Sakhisizwe Local Municipality	Local municipality/ Category B
Senqu Local Municipality	Local municipality/ Category B
Sundays River Valley Local Municipality	Local municipality/ Category B
Tsolwana Local Municipality	Local municipality/ Category B
Umzimvubu Local Municipality	Local municipality/ Category B

2. Municipalities found in the Free State

The following are the municipalities found in the Free State Province of South Africa:

Table B2: Municipalities in the Free State Province:

Name of the municipality	Type of the municipality
Mangaung Metropolitan Municipality	Metropolitan municipality/ Category A
Fezile Dabi District Municipality	District municipality/ Category C
Lejweleputswa District Municipality	District municipality/ Category C
Thabo Mofutsanyana District Municipality	District municipality/ Category C
Xhariep District Municipality	District municipality/ Category C
Dihlabeng Local Municipality	Local municipality/ Category B
Kopanong Local Municipality	Local municipality/ Category B
Letsemeng Local Municipality	Local municipality/ Category B
Mafube Local Municipality	Local municipality/ Category B
Maluti-a-Phofung Local Municipality	Local municipality/ Category B
Mantsopa Local Municipality	Local municipality/ Category B
Masilonyana Local Municipality	Local municipality/ Category B
Matjhabeng Local Municipality	Local municipality/ Category B
Metsimaholo Local Municipality	Local municipality/ Category B
Mohokare Local Municipality	Local municipality/ Category B
Moqhaka Local Municipality	Local municipality/ Category B
Nala Local Municipality	Local municipality/ Category B
Naledi Local Municipality	Local municipality/ Category B
Ngwathe Local Municipality	Local municipality/ Category B
Nketoana Local Municipality	Local municipality/ Category B
Phumelela Local Municipality	Local municipality/ Category B
Setsoto Local Municipality	Local municipality/ Category B
Tokologo Local Municipality	Local municipality/ Category B

Tswelopele Local Municipality	Local municipality/ Category B
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5 Municipalities found in Gauteng Province

The following are the municipalities found in the Gauteng Province of South Africa:

Table B3: Municipalities in Gauteng Province:

Name of the municipality	Type of the municipality
City of Johannesburg Metropolitan Municipality	Metropolitan municipality/ Category A
City of Tshwane Metropolitan Municipality	Metropolitan municipality/ Category A
Ekurhuleni Metropolitan Municipality	Metropolitan municipality/ Category A
Sedibeng District Municipality	District municipality/ Category C
West Rand District Municipality	District municipality/ Category C
Emsfuleni Local Municipality	Local municipality/ Category B
Lesedi Local Municipality	Local municipality/ Category B
Merapong City Local Municipality	Local municipality/ Category B
Midvaal Local Municipality	Local municipality/ Category B
Mogale City Local Municipality	Local municipality/ Category B
Randfontein Local Municipality	Local municipality/ Category B
Westonaria Local Municipality	Local municipality/ Category B

6 Municipalities found in Kwazulu-Natal

The following are the municipalities found in the Kwazulu-Natal Province of South Africa:

Table B4: Municipalities in KwaZulu-Natal Province:

Name of the municipality	Type of the municipality
eThekweni Metropolitan Municipality	Metropolitan municipality/ Category A
Amajuba District Municipality	District municipality/ Category C
eThekweni Metropolitan Municipality	District municipality/ Category C
iLembe District Municipality	District municipality/ Category C

Sisonke District Municipality	District municipality/ Category C
Ugu District Municipality	District municipality/ Category C
uMgungundlovu District Municipality	District municipality/ Category C
uMkhanyakude District Municipality	District municipality/ Category C
uMzinyathi District Municipality	District municipality/ Category C
uThukela District Municipality	District municipality/ Category C
uThungulu District Municipality	District municipality/ Category C
Zululand District Municipality	District municipality/ Category C
Abaqulusi Local Municipality	Local municipality/ Category B
Dannhauser Local Municipality	Local municipality/ Category B
eDumbe Local Municipality	Local municipality/ Category B
eMadlangeni Local Municipality	Local municipality/ Category B
Emnambithi/Ladysmith Local Municipality	Local municipality/ Category B
Endumeni Local Municipality	Local municipality/ Category B
Ezingoleni Local Municipality	Local municipality/ Category B
Greater Kokstad Local Municipality	Local municipality/ Category B
Hibiscus Coast Local Municipality	Local municipality/ Category B
Hlabisa Local Municipality	Local municipality/ Category B
Imbabazane Local Municipality	Local municipality/ Category B
Impendle Local Municipality	Local municipality/ Category B
Indaka Local Municipality	Local municipality/ Category B
Ingwe Local Municipality	Local municipality/ Category B
Jozini Local Municipality	Local municipality/ Category B
KwaDukuza Local Municipality	Local municipality/ Category B
KwaSani Local Municipality	Local municipality/ Category B
Mandeni Local Municipality	Local municipality/ Category B
Maphumulo Local Municipality	Local municipality/ Category B

Mbonambi Local Municipality	Local municipality/ Category B
Mkhambathini Local Municipality	Local municipality/ Category B
Mpofana Local Municipality	Local municipality/ Category B
Msinga Local Municipality	Local municipality/ Category B
Msunduzi Local Municipality	Local municipality/ Category B
Mthonjaneni Local Municipality	Local municipality/ Category B
Mtubatuba Local Municipality	Local municipality/ Category B
Ndwedwe Local Municipality	Local municipality/ Category B
Newcastle Local Municipality	Local municipality/ Category B
Nkandla Local Municipality	Local municipality/ Category B
Nongoma Local Municipality	Local municipality/ Category B
Nquthu Local Municipality	Local municipality/ Category B
Ntambanana Local Municipality	Local municipality/ Category B
Okhahlamba Local Municipality	Local municipality/ Category B
Richmond Local Municipality	Local municipality/ Category B
The Big Five False Bay Local Municipality	Local municipality/ Category B
Ubuhlebezwe Local Municipality	Local municipality/ Category B
Ulundi Local Municipality	Local municipality/ Category B
Umdoni Local Municipality	Local municipality/ Category B
uMhlabuyalingana Local Municipality	Local municipality/ Category B
uMhlathuze Local Municipality	Local municipality/ Category B
uMlalazi Local Municipality	Local municipality/ Category B
uMngeni Local Municipality	Local municipality/ Category B
uMshwathi Local Municipality	Local municipality/ Category B
Umtshezi Local Municipality	Local municipality/ Category B
uMuziwabantu Local Municipality	Local municipality/ Category B
Umvoti Local Municipality	Local municipality/ Category B

Umzimkhulu Local Municipality	Local municipality/ Category B
Umzumbe Local Municipality	Local municipality/ Category B
uPhongolo Local Municipality	Local municipality/ Category B
Vulamehlo Local Municipality	Local municipality/ Category B

7 Municipalities found in Limpopo Province

The following are the municipalities found in the Limpopo Province of South Africa:

Table B5: Municipalities in Limpopo Province:

Name of the municipality	Type of the municipality
Capricorn District Municipality	District municipality/ Category C
Mopani District Municipality	District municipality/ Category C
Sekhukhune District Municipality	District municipality/ Category C
Vhembe District Municipality	District municipality/ Category C
Waterberg District Municipality	District municipality/ Category C
Aganang Local Municipality	Local municipality/ Category B
Ba-Phalaborwa Local Municipality	Local municipality/ Category B
Bela-Bela Local Municipality	Local municipality/ Category B
Blouberg Local Municipality	Local municipality/ Category B
Elias Motsoaledi Local Municipality	Local municipality/ Category B
Ephraim Mogale Local Municipality	Local municipality/ Category B
Fetakgomo Local Municipality	Local municipality/ Category B
Greater Giyani Local Municipality	Local municipality/ Category B
Greater Letaba Local Municipality	Local municipality/ Category B
Greater Tubatse Local Municipality	Local municipality/ Category B
Greater Tzaneen Local Municipality	Local municipality/ Category B
Lepelle-Nkumpi Local Municipality	Local municipality/ Category B
Lephalale Local Municipality	Local municipality/ Category B

Makhado Local Municipality	Local municipality/ Category B
Makhuduthamaga Local Municipality	Local municipality/ Category B
Maruleng Local Municipality	Local municipality/ Category B
Modimolle Local Municipality	Local municipality/ Category B
Mogalakwena Local Municipality	Local municipality/ Category B
Molemole Local Municipality	Local municipality/ Category B
Mookgophong Local Municipality	Local municipality/ Category B
Musina Local Municipality	Local municipality/ Category B
Mutale Local Municipality	Local municipality/ Category B
Polokwane Local Municipality	Local municipality/ Category B
Thabazimbi Local Municipality	Local municipality/ Category B
Thulamela Local Municipality	Local municipality/ Category B

6. Municipalities found in Mpumalanga Province

The following are the municipalities found in the Mpumalanga Province of South Africa:

Table B6: Municipalities in Mpumalanga Province:

Name of the municipality	Type of the municipality
Ehlanzeni District Municipality	District municipality/ Category C
Gert Sibande District Municipality	District municipality/ Category C
Nkangala District Municipality	District municipality/ Category C
Albert Luthuli Local Municipality	Local municipality/ Category B
Bushbuckridge Local Municipality	Local municipality/ Category B
Dipaleseng Local Municipality	Local municipality/ Category B
Dr JS Moroka Local Municipality	Local municipality/ Category B
Emakhazeni Local Municipality	Local municipality/ Category B
Emalahleni Local Municipality	Local municipality/ Category B
Govan Mbeki Local Municipality	Local municipality/ Category B

Lekwa Local Municipality	Local municipality/ Category B
Mbombela Local Municipality	Local municipality/ Category B
Mkhondo Local Municipality	Local municipality/ Category B
Msukaligwa Local Municipality	Local municipality/ Category B
Nkomazi Local Municipality	Local municipality/ Category B
Pixley Ka Seme Local Municipality	Local municipality/ Category B
Steve Tshwete Local Municipality	Local municipality/ Category B
Thaba Chweu Local Municipality	Local municipality/ Category B
Thembisile Hani Local Municipality	Local municipality/ Category B
Umjindi Local Municipality	Local municipality/ Category B
Victor Khanye Local Municipality	Local municipality/ Category B

7. Municipalities found in the North-West Province

The following are the municipalities found in the North-West Province of South Africa:

Table B7: Municipalities in the North-West Province:

Name of the municipality	Type of the municipality
Bojanala Platinum District Municipality	District municipality/ Category C
Dr Kenneth Kaunda District Municipality	District municipality/ Category C
Dr Ruth Segomotsi Mompati District Municipality	District municipality/ Category C
Ngaka Modiri Molema District Municipality	District municipality/ Category C
City of Matlosana Local Municipality	Local municipality/ Category B
Ditsobotla Local Municipality	Local municipality/ Category B
Greater Taung Local Municipality	Local municipality/ Category B
Kagisano-Molopo Local Municipality	Local municipality/ Category B
Kgetlengrivier Local Municipality	Local municipality/ Category B
Lekwa-Teemane Local Municipality	Local municipality/ Category B
Madibeng Local Municipality	Local municipality/ Category B

Mahikeng Local Municipality	Local municipality/ Category B
Mamusa Local Municipality	Local municipality/ Category B
Maquassi Hills Local Municipality	Local municipality/ Category B
Moretele Local Municipality	Local municipality/ Category B
Moses Kotane Local Municipality	Local municipality/ Category B
Naledi Local Municipality	Local municipality/ Category B
Ramotshere Moiloa Local Municipality	Local municipality/ Category B
Ratlou Local Municipality	Local municipality/ Category B
Rustenburg Local Municipality	Local municipality/ Category B
Tlokwe Local Municipality	Local municipality/ Category B
Tswaing Local Municipality	Local municipality/ Category B
Ventersdorp Local Municipality	Local municipality/ Category B

8. Municipalities found in the Northern Cape Province

The following are the municipalities found in the Northern Cape Province of South Africa:

Table B8: Municipalities in the Northern Cape Province:

Name of the municipality	Type of the municipality
Frances Baard District Municipality	District municipality/ Category C
John Taolo Gaetsewe District Municipality	District municipality/ Category C
Namakwa District Municipality	District municipality/ Category C
Pixley ka Seme District Municipality	District municipality/ Category C
ZF Mgcawu District Municipality	District municipality/ Category C
Dikgatlong Local Municipality	Local municipality/ Category B
Emthanjeni Local Municipality	Local municipality/ Category B
Ga-Segonyana Local Municipality	Local municipality/ Category B
Gamagara Local Municipality	Local municipality/ Category B
Hantam Local Municipality	Local municipality/ Category B

Joe Morolong Local Municipality	Local municipality/ Category B
Kai !Garib Local Municipality	Local municipality/ Category B
Kamiesberg Local Municipality	Local municipality/ Category B
Kareeberg Local Municipality	Local municipality/ Category B
Karoo Hoogland Local Municipality	Local municipality/ Category B
Kgatelopele Local Municipality	Local municipality/ Category B
Khâi-Ma Local Municipality	Local municipality/ Category B
!lKhara Hais Local Municipality	Local municipality/ Category B
!Kheis Local Municipality	Local municipality/ Category B
Magareng Local Municipality	Local municipality/ Category B
Mier Local Municipality	Local municipality/ Category B
Nama Khoi Local Municipality	Local municipality/ Category B
Phokwane Local Municipality	Local municipality/ Category B
Renosterberg Local Municipality	Local municipality/ Category B
Richtersveld Local Municipality	Local municipality/ Category B
Siyancuma Local Municipality	Local municipality/ Category B
Siyathemba Local Municipality	Local municipality/ Category B
Sol Plaatje Local Municipality	Local municipality/ Category B
Thembelihle Local Municipality	Local municipality/ Category B
Tsantsabane Local Municipality	Local municipality/ Category B
Ubuntu Local Municipality	Local municipality/ Category B
Umsobomvu Local Municipality	Local municipality/ Category B

9. Municipalities found in the Western Cape Province

The following are the municipalities found in in Western Cape Province of South Africa:

Table B9: Municipalities in the Western Cape Province:

Name of the municipality	Type of the municipality
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City of Cape Town Metropolitan Municipality	Metropolitan municipality/ Category A
Cape Winelands District Municipality	District municipality/ Category C
Central Karoo District Municipality	District municipality/ Category C
Eden District Municipality	District municipality/ Category C
Overberg District Municipality	District municipality/ Category C
West Coast District Municipality	District municipality/ Category C
Beaufort West Local Municipality	Local municipality/ Category B
Bergrivier Local Municipality	Local municipality/ Category B
Bitou Local Municipality	Local municipality/ Category B
Breede Valley Local Municipality	Local municipality/ Category B
Cape Agulhas Local Municipality	Local municipality/ Category B
Cederberg Local Municipality	Local municipality/ Category B
Drakenstein Local Municipality	Local municipality/ Category B
George Local Municipality	Local municipality/ Category B
Hessequa Local Municipality	Local municipality/ Category B
Kannaland Local Municipality	Local municipality/ Category B
Knysna Local Municipality	Local municipality/ Category B
Laingsburg Local Municipality	Local municipality/ Category B
Langeberg Local Municipality	Local municipality/ Category B
Matzikama Local Municipality	Local municipality/ Category B
Mossel Bay Local Municipality	Local municipality/ Category B
Oudtshoorn Local Municipality	Local municipality/ Category B
Overstrand Local Municipality	Local municipality/ Category B
Prince Albert Local Municipality	Local municipality/ Category B
Saldanha Bay Local Municipality	Local municipality/ Category B
Stellenbosch Local Municipality	Local municipality/ Category B
Swartland Local Municipality	Local municipality/ Category B

Swellendam Local Municipality	Local municipality/ Category B
Theewaterskloof Local Municipality	Local municipality/ Category B
Witzenberg Local Municipality	Local municipality/ Category B

ANNEXURE C

RANDOMLY SAMPLED MUNICIPALITIES

Randomly selected municipalities for content analysis (AGSA reports from 2011/2012 – 2015/2016, i.e. 5 AGSA reports per sampled municipality)

Category A municipalities:

Random sampling of five municipalities out of eight municipalities

1. Buffalo City Metropolitan Municipality
2. City of Cape Town Metropolitan Municipality
3. City of Tshwane Metropolitan Municipality
4. City of Johannesburg Metropolitan Municipality
5. Mangaung Metropolitan Municipality

Category B municipalities

Random sampling of 15 municipalities out of 230 municipalities

1. Kouga Local Municipality – Western Cape
2. Mbhashe Local Municipality – Kwazulu Natal
3. KwaDukuza Local Municipality – Kwazulu Natal
4. Emalaheni Local Municipality – Eastern Cape
5. Gariiep Local Municipality – Eastern Cape
6. Letsemeng Local Municipality – Free State
7. Setsoto Local Municipality – Free State
8. Midvaal Local Municipality – Gauteng
9. Polokwane Local Municipality – Limpopo
10. Modimolle Local Municipality – Limpopo
11. Emalaheni Local Municipality – Mpumalanga
12. Lekwa Local Municipality – Mpumalanga
13. Mahikeng Local Municipality – North-West
14. Swellendam Local Municipality –Western Cape
15. George Local Municipality – Western Cape

Category C Municipalities

Random sampling of 10 municipalities out of 47 municipalities

1. West Coast District Municipality – Western Cape
2. Cape Winelands District Municipality – Western Cape
3. Overberg District Municipality – Western Cape
4. Pixley Ka Seme District Municipality – Northern Cape
5. Frances Baard District Municipality – Northern Cape
6. uThukela District Municipality – KwaZulu Natal
7. Ilembe District Municipality – Kwazulu-Natal
8. Alfred Nzo District Municipality – Eastern Cape
9. John Taolo Gaetsewe District Municipality – North West

10. West Rand District Municipality – Gauteng

**ANNEXURE D
ATLAS.TI AUDIT TRAIL
List of codes**

Code-Filter: All

HU: MyPhD
File: [C:\Users\lmamaile\Desktop\MyPhD.hpr7]
Edited by: Super
Date/Time: 2017-08-21 20:56:48

**Mission
MANDATE
INTERNAL AUDIT
Independency
Results of resourced IAF
Role of IAF
Staffing of IAF
Focus of IAF tendency
The establishment of IAF and audit committees
Municipalities without IAFs
Recommendation regarding IAF
Effective governance
Lack of IAFs
MFMA
Treasury regulations
Deficiencies
Root causes
IAFs
Training**

**ANNEXURE E
ATLAS.TI AUDIT TRAIL
Independency**

Report: 1 quotation(s) for 1 code

HU: MyPhD
File: [C:\Users\lmamaile\Desktop\MyPhD.hpr7]
Edited by: Super
Date/Time: 2017-03-22 23:08:18

Mode: quotation list names and references

Quotation-Filter: All

Independency

P 1: 2012_13_Municipalities report 1_general_report.pdf - 1:162 [IAFs assist ac..] (55:3320-55:3574) (Super)

Codes: [independency]

No memos

IAFs assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:42 ! Ensuring that internal audit... (113:43 [113:380])

Ensuring that all actions taken have a strong regard for independence and objectivity.

ANNEXURE F
ATLAS.TI AUDIT TRAIL
Effective governance

Effective governance

Created by Super on 2017/03/14

4 Quotations:

D 23: AGSA_MFMA_MUNICIPALITIES_2011_12 .pdf - 23:47 Effective governance is a key ... (113:129 [113:1000])

Effective governance is a key driver of internal control, which in turn impacts on audit outcomes. Risk management and effective audit committees and IAFs are key elements of this driver of internal control. In terms of the MFMA, all municipalities must establish an audit committee and internal audit unit. Audit committees serve as independent governance structures whose function is to oversee the systems of internal control, compliance with legislation, risk management and all other matters of governance. In executing its duties, the audit committee assists the municipal manager in the effective execution of his/her responsibilities, with the ultimate aim of ensuring that the organisation achieves its objectives. IAFs form an integral part in providing assurance on governance, risk management and internal control.

D 14: AGSA_MFMA_MUNICIPALITIES_2012_13.pdf - 14:20 Effective governance is a key ... (111:129 [111:1020])

Effective governance is a key driver of internal control, which impacts on audit outcomes. Risk management and effective audit committees and IAFs are key elements of this driver of internal control. In terms of the MFMA, an audit committee and internal audit unit must be established by all auditees. Audit committees serve as independent governance structures whose function is to play an oversight role regarding the systems of internal control, compliance with legislation, risk management and all other matters of governance. In executing its duties, the audit committee assists the accounting officer in the effective execution of his/her responsibilities, with the ultimate aim of ensuring that the organisation achieves its objectives. IAFs form an integral part in providing assurance on governance, risk management and internal control.

D 14: AGSA_MFMA_MUNICIPALITIES_2013_14.pdf - 14:24 A functional internal audit un... (112:82 [112:553])

A functional internal audit unit, systems of internal control and effective operation of an audit committee are crucial components for sound corporate governance at municipalities. The MFMA requires that these financial governance components exist within all municipalities and municipal entities.

D 14: AGSA_MFMA_MUNICIPALITIES_2013_14.pdf - 14:30 Certain municipalities also un... (113:82 [113:671])

Certain municipalities also undermine the importance of the audit committees and IAFs and exist mainly for compliance with legislation and the potential value they have in ensuring sound governance is not fully realised. Internal audit findings and recommendations by the audit committees are not responded to timeously or recommendations are rarely implemented. It is the implementation of recommendations rather than the recommendation as such that drives improved systems of internal control, monitoring and supervision and, ultimately, improved outcomes.

ANNEXURE G
ATLAS.TI AUDIT TRAIL
Lack of IAFs

○ **Lack of IAFs**

Created by Super on 2017/03/14

3 Quotations:

D 23: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 23:48 A number of municipalities (14%) municipalities did... (119:1818 [119:2069])

A number of municipalities (14%) did not implement IAFs. It must further be noted that none of the other 19 (86%) municipalities had implemented an internal audit unit that was fully effective and provided the required level of assurance.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:88 is reliable and complete. The ... (156:4077 [156:4249])

The IAFs were only in place for a part of the year and were not able to address all risks or produce all the necessary reports required.

D 14: AGSA_MFMA_MUNICIPALITIES_2013_14.pdf - 14:30 Certain municipalities also un... (113:82 [113:671])

Certain municipalities also undermine the importance of the audit committees and IAFs and exist mainly for compliance with legislation and the potential value they have in ensuring sound governance is not fully realised. Internal audit findings and recommendations by the audit committees are not responded to timeously or recommendations are rarely implemented. It is the implementation of recommendations rather than the recommendation as such that drives improved systems of internal control, monitoring and supervision and, ultimately, improved outcomes.

ANNEXURE H
ATLAS.TI AUDIT TRAIL
The AGSA mandate

o **MANDATE**

Created by Super on 2017/03/07

3 Quotations:

D 1: 2012_13_MFMA_MUNICIPALITIES_report.pdf - 1:2 Auditor-General of South Afric... (3:40 [3:234])

Auditor-General of South Africa has a constitutional mandate and, as the Supreme Audit Institution (SAI) of South Africa, exists to strengthen our country's democracy by enabling oversight.

D 14: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 14:6 The PAA requires the AGSA to a... (46:81 [46:831])

The PAA requires the AGSA to audit on an annual basis compliance with laws and regulations applicable to financial matters, financial management and other related matters. The compliance audit was limited to the following focus areas: Material misstatements in submitted annual financial statements Asset and liability management Audit committees Budget management Expenditure management Prevention of unauthorised, irregular as well as fruitless and wasteful expenditure Financial misconduct Internal audit Revenue management Strategic planning and performance management Transfer of funds and conditional grants Procurement and contract management (supply chain management) Human resource management and compensation.

D 17: AGSA_MFMA _ MPUMALANGA_2011_12.pdf - 17:10 The Public Audit Act requires ... (33:1128 [33:1896])

The Public Audit Act requires us to audit compliance with laws and regulations applicable to financial matters, financial management and other related matters each year. The compliance audit was limited to the following focus areas: ■ material misstatements in the submitted annual financial statements ■ asset and liability management ■ audit committees ■ budget management ■ expenditure management ■ prevention of unauthorised, irregular as well as fruitless and wasteful expenditure ■ financial misconduct ■ internal audit ■ revenue management ■ strategic planning and performance management ■ transfer of funds and conditional grants ■ procurement and contract management, or supply chain management (SCM) ■ human resource (HR).

**ANNEXURE I
ATLAS.TI AUDIT TRAIL**

Recommendations regarding the IAF

○ **Recommendations regarding IAF**

Created by Super on 2017/03/13

9 Quotations:

D 26: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 26:63 The leadership needs to contin... (106:350 [106:635])

The leadership needs to continue to keep their focus on fully functioning IAFs so that sufficient assurance in the areas of financial reporting, predetermined objectives, and compliance with laws and regulations can translate into positive impact on audit outcomes.

D 1: 2012_13_MFMA_Municipality_general_report.pdf - 1:8 • Building internal audit capa... (32:733 [32:808])

Building internal audit capacity to enable the IAF.

D 2: AGSA_MFMA_Municipalities_2012_13.pdf - 2:39 Ensure that an adequately reso... (113:143 [113:325])

Ensure that an adequately resourced and functioning internal audit unit is in place that identifies internal control deficiencies and recommends corrective action effectively.

D 1: 2013_14_MFMA_Municipalities_general_report.pdf - 1:12 • Ensure that an adequately re... (55:1272 [55:1348])

Ensure that an adequately resourced and functioning IAFs exist at municipalities.

D 2: AGSA_MFMA_Municipalities_2013_14.pdf - 2:36 The municipal leadership shoul... (104:1107 [104:1246])

The municipal leadership should respond appropriately to requests for information and comments on findings raised by the IAFs.

D 2: AGSA_MFMA_Municipalities_2014_15.pdf - 2:35 The leadership should ensure t... (104:846 [104:1058])

The leadership should ensure that sufficient resources are made available to the audit committees and IAFs for them to assist in improving governance in the local government sector.

D 5: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 5:20 Ensure that an adequately reso... (90:1755 [90:1937])

Ensure that an adequately resourced and functioning internal audit unit is in place that identifies internal control deficiencies and recommends corrective action effectively.

D 5: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 5:45 Strengthen the role of the int... (131:890 [131:995])

Strengthen the role of the internal audit unit by assisting the units to develop risk-based audit plans.

D 7: 2012-13 MFMA_Municipalities_ general report2.pdf - 7:239 For improved audit outcomes th... (276:4082 [276:4915])

For improved audit outcomes, the assurance levels should be improved. This should be achieved by ensuring stability at the level of senior management, fast-tracking the timelines of delivery by internal audit, and directing the audit committee towards evaluating performance information, financial reporting and supply chain management.

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:42 ! Ensuring that internal audit... (113:43 [113:380])

Ensuring that internal audits are conducted in compliance with the Internal Audit Standards;

Ensuring that the internal audit is fully resourced by staff and technology;

Ensuring that the internal audit plan is completed; and

Ensuring that all actions taken have a strong regard for independence and objectivity.

D 11: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 11:36 Action plans developed to addr... (95:1134 [95:1561])

Action plans developed to address the external and internal audit findings should be clear, precise and time bound, and responsibilities should be assigned with monitoring mechanisms to ensure effectiveness. Internal audit should provide continued assurance on the effective implementation of the action plans. Progress towards implementation of the action plans should form part of agenda items at audit committee meetings.

ANNEXURE J
ATLAS.TI AUDIT TRAIL
Results of resourced IAF

○ **Results of resourced IAF**

Created by Super on 2017/03/13

2 Quotations:

D 1: 2012_13_MFMA_MUNICIPALITIES_general_report.pdf - 1:163 In many instances, we have see... (55:192 [56:4562])

- “Provide effective and ethical leadership, and oversee financial and performance reporting and compliance with legislation.
- Implement effective HR management to ensure that adequate and sufficiently skilled staff are employed.
- Set the correct tone to improve the performance and productivity of staff by implementing sound performance management processes, evaluating and monitoring performance, and imposing proper consequences for poor performance.
- Establish policies and procedures to enable sustainable internal control practices, and monitor the implementation of action plans to address internal control deficiencies.
- Establish an IT governance framework that supports and enables the achievement of objectives, delivers value and improves performance.
- Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of IT risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.
- Ensure that an adequately resourced and functioning internal audit unit is in place and that internal audit reports are responded to.
- Support the audit committee and ensure that its reports are responded to”.

Mayor

Framework scenario: “Mayors have a monitoring and oversight role at both municipalities and municipal entities. They have specific oversight responsibilities in terms of the MFMA and the MSA, which include reviewing the integrated development plan and budget management as well as ensuring that auditees address the issues raised in audit reports. Mayors can bring about improvements in the audit outcomes of their auditees by being actively involved in key governance matters and managing the performance of the accounting officers and authorities”.

As information presented by senior management was not credible, mayors were unable to make informed decisions based on sound financial information. Mayors have therefore not

provided the required level of assurance, which was also confirmed through our interactions with them. The mayors should implement corrective action where necessary, as it remains their responsibility to enforce accountability from the top down.

Over the past three years, we have increasingly engaged with mayors on how they can improve the audit outcomes of their municipalities. This includes discussing the status of key controls and mayoral commitments to improve audit outcomes, while also sharing identified risks. At an overall level, these interactions were well received but their impact depended on the political will of the mayors concerned and their commitment to change. Those mayors who were responsive towards our messages and implemented our recommendations made improvements in the levels of assurance provided and ultimately their audit outcome”.

Going forward, a decisive and proactive leadership tone is required to instil a culture of accountability and good governance.

“Internal audit and audit committee Framework scenario: IAFs assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.

Framework scenario: “An audit committee is an independent body that advises the council, mayor, accounting officer or authority and senior management on matters such as internal controls, risk management, performance management, evaluation and compliance with legislation. The committee is required to provide assurance to the council on the adequacy, reliability and accuracy of financial reporting and performance information”.

While we previously credited the province for the establishment of, and investment in, IAFs and audit committees, the impact on audit outcomes and the assurance provided by these very important role players have been fairly limited.

It is clear that the effectiveness of these structures is hampered by poor resourcing relating to the availability and competence of people serving in these structures and the lack of reaction to the work and reports of these structures by the assurance providers on the first level.

“In many instances, we have seen the positive effect that well-resourced and active IAFs and audit committees can have on the improvement of internal controls within an auditee. Mayors, municipal managers and senior management are urged to recognise these structures as key partners in the General report on the audit outcomes of Eastern Cape local government for accountability chain, to resource these structures appropriately, and to react seriously to their work”.

Provincial Treasury, Office of the Premier and Department of Local Governance and Traditional Affairs. The Constitution stipulates that provincial government must support and strengthen the capacity of municipalities to manage their own affairs, to exercise their powers, and to perform their duties. The MFMA further requires provincial government to assist municipalities in building capacity to support efficient, effective and transparent financial management. Both the MFMA and the MSA define responsibilities to monitor financial and performance management in compliance with these acts.

The provincial departments that have a direct role to play in supporting and monitoring local government, and thereby providing a level of assurance, are the Provincial Treasury, the Department of Local Governance and Traditional Affairs and the Office of the Premier. Our assessment of the assurance provided by these departments is based on their initiatives to support and monitor local government and the impact they have had on improving the internal controls of auditees.

“The principal role player in the drive towards clean administration is the Department of Local Governance and Traditional Affairs. The department has focused on municipalities through its operation clean audit (OCA) unit, specifically at those municipalities that had previously received adverse and disclaimed audit opinions. The outcomes of OCA interventions are detailed further on in this report.

Municipal council and municipal public accounts committee Framework scenario: The council is required to provide assurance through monitoring and oversight. This includes approving or overseeing certain transactions and events as well as investigating and acting on poor performance and transgressions, such as financial misconduct and unauthorised, irregular as well as fruitless and wasteful expenditure.

Framework scenario: MPACs were introduced as a committee of the council to deal specifically with the municipality’s annual report, financial statements and audit outcomes, and to improve governance, transparency and accountability. The committee is an important provider of assurance, as it needs to give assurance to the council on the credibility and reliability of financial and performance reports, compliance with legislation as well as internal controls.

Councillors did not adhere to their basic responsibilities, which calls into question their effectiveness. Councillors lacked the necessary training to perform their duties effectively and as a result did not fulfil the roles expected of them by legislation and the citizens of their constituencies. The Standing Committee on Public Accounts opened its doors to any MPAC member who wanted to observe hearings and learn from experience how they should conduct MPAC hearings.

The Association of Public Accounts Committees has also been active in training councillors on oversight functions. These interventions are relatively new and have thus not yet achieved their full impact. We further analysed MPACs to determine why they were not able to provide the required level of assurance. MPACs must hold four meetings per year, but Figure 38 indicates that almost a quarter of MPACs did not hold the required number of meetings.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:17 In many instances, we have see... (55:4555 [55:4863])

In many instances, we have seen the positive effect that well-resourced and active IAFs and audit committees can have on the improvement of internal controls within an auditee. Mayors, municipal managers and senior management are urged to recognise these structures as key partners in their day to day operations.

ANNEXURE K
ATLAS.TI AUDIT TRAIL
Role of IAF

○ **Role of IAF**

Created by Super on 2017/03/13

4 Quotations:

D 22: 2012_13_MFMA_MUNICIPALITIES_general_report.pdf - 22:130 IAFs assist mu... (30:2741 [30:2976])

IAFs should assist municipal managers in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.

D 1: 2013_14_MFMA_MUNICIPALITIES_general_report.pdf - 1:4 Municipal public accounts comm... (21:1881 [21:2022])

Municipal public accounts committees (MPACs), audit committees and IAFs should assist councils to make informed decision.

D 5: AGSA_MFMA_MUNICIPALITIES_2014_15.pdf - 5:24 Effective governance is a key ... (115:135 [115:1041])

Effective governance is a key driver of internal control, which in turn impacts audit outcomes. Risk management and effective audit committees and IAFs are key elements of this driver of internal control. In terms of the MFMA, an audit committee and internal audit unit must be established by all auditees. An audit committee serves as an independent governance structure whose function is to play an oversight role in respect of the systems of internal control, compliance with legislation, risk management and all other matters of governance. In performing its duties, the audit committee assists the accounting officer in the effective execution of his/her responsibilities, with the ultimate aim of ensuring that the organisation achieves its objectives. IAFs form an integral part of providing assurance on governance, risk management and internal control.

D 7: 2012-13 MFMA_Municipalities general report2.pdf - 7:36 The audit committee and intern... (67:2774 [67:2930])

The audit committee and internal audit should review all critical accounting areas to ensure that they are correctly applied.

D 7: 2012-13 MFMA_Municipalities_ general report2.pdf - 7:50 internal audit and audit commi... (80:4045 [80:4195])

The internal audit and audit committee should focus on improving the quality of financial statements and reported performance.

ANNEXURE L
ATLAS.TI AUDIT TRAIL
Staffing of IAF

Staffing of IAF

Created by Super on 2017/03/13

11 Quotations:

D 2: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 2:4 • Weak or understaffed internally... (23:1190 [23:1232])

Weak or understaffed IAFs.

D 22: 2012_13_MFMA_MUNICIPALITIES_general_report.pdf - 22:131 The IAFs at 79... (30:3270 [30:3668])

The IAFs at 79% of the municipalities are not adequate and effective. It was further noted that IAFs are not adequately staffed and, where positions are filled, the officials lack the required skills. It is recommended that district municipalities implement effective shared IAFs that can assist the local municipalities with proper oversight.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:114 discharge their responsibilities... (188:3715 [188:3939])

The assurance provided was further negatively affected by the capacity constraints within the internal audit unit and the resultant impact on audit committee responsibility.

D 7: 2013_14_MFMA_Municipalities_report2.pdf - 7:113 Ensure adequate staffing of th... (147:1578 [147:1638])

Ensure adequate staffing of the shared IAFs.

D 2: AGSA_MFMA_MUNICIPALITIES_2014_15.pdf - 2:32 Governance structures were not... (103:1316 [103:1615])

Governance structures were not adequately equipped in terms of financial, human and other resources. In addition, the leadership did not adequately support the work of IAFs and audit committees, as required documentation was not provided and management reports were not responded to.

D 4: 2012_13_MFMA_Municipalities_general_report.pdf - 4:10 IAFs can only ... (29:4540 [29:4621])

IAFs can only be effective if they are adequately resourced.

D 5: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 5:43 IAFs were not ... (124:122 [124:482])

IAFs were not always fully capacitated with skilled, experienced staff. Although IAFs exist in most cases, the control environment will be compromised if their findings are ignored or not taken seriously, which ultimately reduces the level of assurance that can be placed on financial information and the control environment.

D 7: 2012-13 MFMA_Municipalities_general report2.pdf - 7:237 The lack of significant improv... (276:2174 [276:2398])

The lack of significant improvement in the key controls was caused by the governance structures having regressed due to the lack of capacity in IAFs, which has affected the operations of the audit committee.

D 8: AGSA_MFMA_MUNICIPALITIES_2013_14.pdf - 8:42 ! Ensuring that internal audit... (113:43 [113:380])

Ensuring that the internal audit is fully resourced by staff and technology.

D 11: AGSA_MFMA_MUNICIPALITIES_2014_15.pdf - 11:49 • Lack of technical capacity a... (129:2288 [129:2338])

Lack of technical capacity at internal audit unit

D 23: AGSA_MFMA_MUNICIPALITIES_2015_16.pdf - 23:23 The province was struggling to... (86:1480 [86:2021])

The municipalities were struggling to find sufficiently competent and experienced individuals to staff the IAFs in the provinces, which resulted in IAFs not having sufficient capacity to perform their required functions. The units could therefore not promote accountability and service delivery through evaluating and monitoring responses to risks and providing oversight of the effectiveness of the internal control environment, including financial and performance reporting and compliance.

ANNEXURE M
ATLAS.TI AUDIT TRAIL
Establishment of IAF

○ **The establishment of IAF and audit committees**

Created by Super on 2017/03/13

4 Quotations:

D 26: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 26:61 Effective governance is a key ... (99:54 [99:951])

Effective governance is a key driver of internal control, which in turn impacts on audit outcomes. Risk management and effective audit committees and IAFs are key elements of this driver of internal control. In terms of the MFMA, an audit committee and internal audit unit must be established by all auditees. Audit committees serve as independent governance structures whose function is to play an oversight role regarding the systems of internal control, compliance with legislation, risk management and all other matters of governance. In executing its duties, the audit committee assists the accounting officer in the effective execution of his/her responsibilities, with the ultimate aim of ensuring that the organisation achieves its objectives. IAFs form an integral part in providing assurance on governance, risk management and internal control.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:54 Although the internal audit un... (116:4166 [116:4478])

Although the internal audit unit and audit committee fully fulfilled their role, management's failure to attend to internal audit findings and to respond to the audit committee's recommendations had a negative impact on the ability of other assurance providers to execute their responsibilities effectively.

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:22 Audit committees and internal ... (110:756 [110:1090])

Audit committees and IAFs should be fully compliant with laws and regulations governing them as part of the execution of their mandates. The audit outcomes reflect that 14% of the audit committees as well as 6% of the IAFs were not fully compliant.

D 25: 2012_13_MFMA_MUNICIPALITIES_general_report.pdf - 25:98 Lack of skills and competencie... (133:2110 [133:2360])

Lack of skills and competencies: Individuals with the necessary skills, competencies and knowledge were not employed in critical positions in the finance unit and performance management units while an internal audit unit was not established in some municipalities.

ANNEXURE N
ATLAS.TI AUDIT TRAIL
Tendency of IAF

○ **Focus of IAF tendency**

Created by Super on 2017/03/13

3 Quotations:

D 24: MFMA 2013-14 MUNICIPALITIES.pdf - 24:24 A concern with some shared int... (52:2107 [52:2489])

A concern with some shared IAFs remains that they tend to focus their efforts too much on the district municipality where they are based and perform significantly less work at the local municipalities in their districts. The responsiveness of management at the local municipalities plays a role in the area where the internal audit unit will focus its efforts.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:57 providers to discharge their r... (120:3897 [120:4134])

The IAFs and audit committees did not receive adequate information to execute their responsibilities effectively, and their recommendations were not implemented.

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:36 It is clear from the results t... (111:2053 [111:2558])

It is clear from the results that a large extent of audit committees and IAFs devoted attention to ensuring compliance with laws and regulations and SCM requirements. However, the depth of the work needs to be more focused and risk based to ensure that key issues that have a financial impact and public interest are highlighted.

ANNEXURE O
ATLAS.TI AUDIT TRAIL
Findings on IAF and MFMA

○ **Findings regarding IAF and MFMA**

Created by Imamaile on 2017/10/09

9 Quotations:

D 4: Municipalities_ Audit report 2011-12 - 4:1 Internal Audit 33. The internal audit unit did not function as re... (7:1662 [7:3057])

33. The internal audit unit did not function as required by section 165(2) of the Municipal Finance Management Act, in that it did not advise the accounting officer on matters relating to accounting procedures and practices and risk management.

34. The internal audit unit did not report to the audit committee on matters relating to the compliance with the Municipal Finance Management Act, the Division of Revenue Act and other applicable legislation, as required by section 165(2)(b) of the Municipal Finance Management Act.

35. The internal audit did not audit the results of performance measurements, as required by section 45(1)(a) of the Municipal Systems Act and Municipal Planning and Performance Management Regulation 14(1)(a).

36. The internal audit unit did not assess the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal Planning and Performance Management Regulation 14(1)(b)(ii) and (iii).

37. The internal audit unit did not audit the performance measurements on a continuous basis and submitted quarterly reports on their audits to the municipal manager and the performance audit committee, as required by Municipal Planning and Performance Management Regulation 14(1)(c).

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:31 Internal audit Provides limited... (87:705 [87:748])

Internal audit provided limited/no assurance to the municipalities.

D 1: 2013_14_MFMA_Municipalities_general_report.pdf - 1:51 limited. This can be improved ... (112:4396 [112:4601])

The level of assurance provided by the audit committee and IAFs was limited. This can be improved if the internal audit unit is better used and directed. To pave the way forward, all role players need to work together towards an environment that promotes accountability.

D 1: 2014_15_MFMA_Municipalities_report.pdf - 1:41 We met with the mayor three ti... (100:3812 [100:4246])

The audit committee and internal audit unit only provided some assurance. This can be improved if management responds more effectively to the committee's recommendations in internal audit reports.

D 2: AGSA_MFMA_MUNICIPALITIES_2014_15.pdf - 2:16 The audit committees and inter... (62:1008 [62:1268])

The audit committees and IAFs did not always respond effectively to the non-compliance risks identified, resulting in many instances of non-compliance (especially regarding SCM) being identified for the first time during the audit process.

D 1: 2015_16_MFMA_Municipalities.pdf - 1:25 The internal audit unit and au... (76:3889 [76:4563])

The internal audit unit and audit committee were fully functional, but provided limited assurance, as management did not adequately respond to their recommendations.

D 1: 2015_16_MFMA_Municipalities_general_report.pdf - 1:71 The internal audit unit and au... (136:3739 [136:4237])

The internal audit unit and audit committee did not provide adequate assurance, due to the delay in implementing the audit plan. Going forward, the internal audit unit should ensure that all key risk areas are addressed in their audit plan and prioritised.

D 5: AGSA_MFMA_Municipalities_2011_12.pdf - 5:30 • In total, 16 (67%) audit com... (116:633 [116:754])

In total, 16 (67%) audit committees and 15 (65%) IAFs did not meet all the legislated requirements.

D 11: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 11:2 Internal audit plans were not ... (16:869 [16:1087])

Internal audit plans were not designed and aligned to address the fundamental weaknesses in the internal control environment; as a result, the audit work performed had minimal impact on improving audit outcomes.

Establishment of IAF and audit committees

D 1: 2011_12_MFMA_Municipalities_general_report.pdf - 1:44 The senior leadership of the m... (104:3524 [104:3944])

“The senior leadership of the municipality provided limited or no assurance, which directly affected the credibility of the information produced and the ability of the other assurance providers to discharge their responsibilities effectively. This is illustrated by the fact that the established internal audit unit and audit committee were also not deemed completely effective, as management did not improve on their operations within the municipalities”.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:88 is reliable and complete. The ... (156:4077 [156:4249])

The IAFs were only in place for a part of the year and were not able to address all risks or produce all the necessary reports required.

D 1: 2012_13_MFMA_Municipalities_general_report.pdf - 1:47 responsibilities. The internal... (108:3672 [108:3841])

The internal audit unit and audit committee did not receive the necessary support and information to execute their responsibilities effectively.

D 1: 2013_14_MFMA_Municipality_general_report.pdf - 1:80 The internal audit unit and au... (144:3723 [144:3964])

The internal audit unit and audit committee only provided some assurance, as their focus was limited. They did not timeously address the key risks at the municipality and did not provide sufficient assurance on service delivery reports.

D 2: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 2:41 E? ective governance is a key ... (124:1862 [124:2773])

Effective governance is a key driver of internal control, which – in turn – has an impact on audit outcomes. Risk management and effective audit committees and IAFs are key elements of this driver of internal control. In terms of the MFMA, all auditees must establish an audit committee and internal audit unit. Audit committees serve as independent governance structures whose function it is to play an oversight role regarding the systems of internal control, compliance with legislation, risk management and all other matters of governance. In executing its duties, the audit committee assists the accounting officer in the effective execution of his or her responsibilities, with the ultimate aim of ensuring that the auditee achieves its objectives. IAFs are an integral part in providing assurance on governance, risk management and internal control.

D 4: 2012_13_MFMA_Municipality_general_report.pdf - 4:77 To improve the audit outcome t... (124:3715 [124:4099])

To improve the audit outcome the assurance level should be enhanced by establishing adequate capacity to address internal control weaknesses, as indicated above. Senior management should ensure that the recommendations of the Auditor-General and internal audit are timeously implemented and that the work of the audit committee is directed towards evaluating significant matters.

ANNEXURE Q
ATLAS.TI AUDIT TRAIL
Deficiencies

D 2: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 2:2 • The lack of adequate progres... (21:2389 [21:2710])

The lack of adequate progress can be attributed to inadequate oversight by those charged with governance, a lack of consequences for not resolving audit findings, and a lack of consistent monitoring by IAFs and audit committees of the progress made in implementing management.

D 5: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 5:43 IAFs were not ... (124:122 [124:482])

IAFs were not always fully capacitated with skilled, experienced staff. Although IAFs exist in most cases, the control environment will be compromised if their findings are ignored or not taken seriously, which ultimately reduces the level of assurance that can be placed on financial information and the control environment.

D 6: MFMA 2013-14 Municipalities.pdf - 6:2 All role players did not provi... (20:812 [20:1324])

All role players did not provide the required level of assurance. As a result, the financial statements and annual performance reports prepared, reviewed and signed off by the auditees' senior management and municipal managers/chief executive officers were materially misstated. The IAFs and, in most cases, the audit committees also did not add to the credibility of these reports, while monitoring and oversight by the political leadership.

D 7: 2012-13 MFMA_Municipalities_ general report2.pdf - 7:10 The level of assurance provide... (34:555 [34:2490])

The assurance provided by internal audit is affected by the lack of effective and/or standardised methodologies and practice manuals. In many instances, the level of knowledge and proficiency in the local government space of internal auditors is often deficient. Capacity constraints and limited budgets further affect the ability of internal auditors to conduct their audits in a manner codified by the Institute of Internal Auditors as the required supervision, reviews and training cannot take place as expected. As a result, the necessary risk areas are sometimes not addressed by internal audit, delays arise in the finalisation of reports and the expectations of leadership are not met. Another major hurdle that affects the assurance derived from internal audit is the commitment of leadership to appreciate the importance of an IAF and to promptly implement their recommendations. This lack of commitment in many instances frustrates the internal audit unit and leads to vacancies or reduced efforts by internal auditors.

To uphold the ethos of local government, the political and administrative leadership need to direct more effort into building the capacity and skills of internal auditors to strengthen control environments and proactively manage risks. This will also enable internal audits to be done throughout the year to focus on root causes and control weakness that need to be remedied. Heads of internal audit should also have full access to report to MPAC and council on their audit results, free of any reprisal, to enable leadership to be fully appraised of the status of administrations under their stewardship for informed decisions to be taken.

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:40 The regression in audit outcom... (112:834 [112:3147])

The regression in audit outcomes is indicative of the fact that audit committees as well as IAFs do not have a positive impact on the audit outcomes of certain auditees. In this regard, audit committees and internal auditors were not swift enough to identify material misstatements in financial statements before the submission thereof for auditing purposes. This is because their risk assessments and responses were not proactive to timeously address imminent performance management, technical as well as compliance issues, thus undermining the reliability and integrity of reporting.

ANNEXURE R
ATLAS.TI AUDIT TRAIL

Root causes

D 3: MFMA 2013-14 Municipalities.pdf - 3:17 The impact on audit outcomes a... (54:3300 [54:4128])

The impact on audit outcomes and the assurance provided by these pivotal role players have been limited. It is clear that the effectiveness of these structures is hampered by poor resourcing and management not responding to their work and reports. Repetitive findings and the failure to address root causes also raise the question of whether IAFs and audit committees are focusing their efforts on risk management and on improving the systems to enhance the credibility of information through implementing the necessary controls. Going forward, risk assessments should ensure that the proper weighting is assigned to this area, while responses to those risk assessments should be focused on systems and controls that entrench the credibility of information in the daily functioning of the municipalities.

ANNEXURE S
ATLAS.TI AUDIT TRAIL
Treasury regulations

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:22 Audit committees and internal ... (110:756 [110:1090])

Audit committees and IAFs should be fully compliant with laws and regulations governing them as part of the execution of their mandates. The audit outcomes reflect that 14% of the audit committees as well as 6% of the IAFs were not fully compliant.

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:42 ! Ensuring that internal audit... (113:43 [113:380])

Ensuring that internal audits are conducted in compliance with the Internal Audit Standards;

ANNEXURE T
ATLAS.TI AUDIT TRAIL
Mission of IAF

D 8: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 8:39 The primary objective of inter... (112:123 [112:831])

The primary objective of internal audit unit is to provide assurance to the leadership, management and the audit committee, amongst others, on whether internal controls are designed, implemented and maintained in a manner that provides and promotes business risk insights, value protection and creation and risk mitigation. The internal audit unit should be able to meet the changing needs of local government as well as the business strategies thereof and should be aligned to the expectations of management and the audit committee. The audit committee, in turn, based on effective internal audit support, should be able to provide reliable and credible reports to municipal leadership.

ANNEXURE U
ATLAS.TI AUDIT TRAIL

Training

D 11: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 11:55 Internal audit methodology is ... (129:3359 [129:3692])

Internal audit methodology is not aligned to AGSA audit of PDO methodology and thus hampering the effectiveness in evaluating the reliability and usefulness of PDO reports. The skills and capacity of the governance structures need to be enhanced through continuous training in order to ensure robust oversight is discharged.

D 11: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 11:64 IAFs were not ... (137:311 [137:836])

IAFs were not adequately capacitated, resulting in ineffective assurance, advisory and reporting functions. There was a shortage of appropriate technically skilled auditors. Although we had provided training to IAFs on PDO reporting, no significant improvement can be seen in the outcomes. Risk assessments were not aligned to the regularity audit focus areas and as a result findings still arose on non-compliance with laws and regulations and PDOs, which prevented clean audit outcomes.

D 11: AGSA_MFMA_MUNICIPALITIES_2011_12.pdf - 11:65 The above scenarios contribute... (137:839 [137:1110])

The above scenarios contributed to poor quality internal audit reports. As a result, recommendations were not taken seriously by management. IAFs also did not add credibility to the financial reporting process nor to the quarterly review of key controls.

D 23: AGSA_MFMA_MUNICIPALITIES_2015_16.pdf - 23:23 The province was struggling to... (86:1480 [86:2021])

The municipalities were struggling to find sufficiently competent and experienced individuals to staff the IAFs in the provinces, which resulted in IAFs not having sufficient capacity to perform their required functions. The units could therefore not promote accountability and service delivery through evaluating and monitoring responses to risks and providing oversight of the effectiveness of the internal control environment, including financial and performance reporting and compliance.

D 25: 2012_13_MFMA_MUNICIPALITIES_general_report.pdf - 25:98 Lack of skills and competencie... (133:2110 [133:2360])

Lack of skills and competencies: Individuals with the necessary skills, competencies and knowledge were not employed in critical positions in the finance unit and performance management units while an internal audit unit was not established in some municipalities.

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