

**REPORT OF THE AUDIT COMMITTEE OF THE NELSON MANDELA BAY MUNICIPALITY –
PERIOD ENDED 31 AUGUST 2017**

OBJECTIVE

The purpose of this report is to present the Audit Committee's review in respect of carrying out its oversight responsibilities, including oversight of the draft financial statement review for the financial year ended 30 June 2017.

The municipal elections of 2016 with the resultant rescheduling of the AC meeting to later in the year, saw one report being issued in January. This report covers the period through to the review of the AFS in August.

TERMS OF REFERENCE

The mandate of the Audit Committee is legislated in terms of section 166 of the Municipal Finance Management (MFMA) Act, 2003 which requires the Audit Committee to advise the Accounting officer and Council on matters relating to:

- Internal financial control and internal audits
- Risk Management adequacy
- Reliability and accuracy of financial reporting and information
- Accounting policies
- Performance Management and evaluation
- Effective Governance
- Compliance with the MFMA, the Annual Division of Revenue Act (DORA) and other applicable legislation and / or policies together with other matters referred to it by the Municipality.

The Audit Committee is also required to fulfill the functions of a Performance Management Committee constituted in terms of Regulation 14(2) of the Local Government: Municipal Planning and Performance Management Regulations, 2001.

The Audit Committee reviewed the Performance Management report at each Audit Committee meeting, where the minutes of the meeting are circulated to council.

The MFMA also requires the Audit Committee to review the annual financial statements, respond to Council on matters raised by the Auditor General and carry out investigations into the financial affairs of the Municipality.

1. Internal Audit and Risk Assurance

- The Audit Committee has reviewed the three year rolling strategic plan compiled by Internal Audit together with the annual Internal Audit plan. The annual Internal Audit plan has been prepared taking cognisance of those identified high residual risks identified by the Risk Management Unit, in consultation with the various Municipal Directorates.
- The Audit Committee has assessed the annual internal Audit plan where the scope of internal audit work planned will assist in improving the effectiveness of risk management, control and governance of processes.
- High risks identified through Internal Audit and the Auditor General are maintained on a high risk register. Insufficient progress is being made in effectively implementing recommendations as set out in assurance reports. As a result, repeat findings continue to be reported on with the Municipality operating in a less optimal control environment. The Audit Committee recommends that a focused approach on addressing high risk findings be undertaken with targeted dates scheduled to address specific noted findings.
- The Audit Committee Chairperson together with Internal Audit Director have met with MPAC Chairperson and City Manager to assist in addressing outstanding high risk findings.
- Effectively implementing those recommendations made in respect of assurance reports issued will see lower instances of reported Irregular, fruitless and wasteful expenditure. In addition, the risk of fraud and error may be reduced by strengthening the control environment.
- A limitation of scope in respect of internal audits conducted is a repeated finding within numerous assurance reports issued. Every effort should be made to ensure Management are working with Internal Audit at the point of internal audits being undertaken to ensure a limitation of scope is not a reported finding.
- Internal Audit completed in excess of 93% of the annual audit plan for the 2016/17 year where internal assurance reports had been issued.
- Internal Audit update the audit plan on a quarterly basis and present the updated plan to the Audit Committee at each quarterly meeting, allowing the Audit Committee to comment on progress together with changes in the annual plan.
- The Audit Committee notes an improved working relationship between Municipal Directorate Management and Internal Audit. Management should continue to ensure that they always understand and agree with the findings of assurance reports issued. Recommendations set out per assurance reports should be reviewed with the Executive Management together with the directors of each relevant Directorate for which an assurance report is prepared. Recommendations must be agreed to by all Senior Management personnel and must be implemented to mitigate future high risk findings.

- The implementation of mSCOA is currently not meeting the implementation deadline dates. Budget and Treasury should advise council as to the relevant circumstances as they exist and highlight the specific risks that may be realised where the implementation of mSCOA does not meet the deadline dates as set by National Treasury.
- Concern had previously been noted with the pending expiry of the Internal Audit co-sourced service provider. This risk has been mitigated through the extension of the co-sourced service provider's contract for a period of one year, while internal capacity within Internal Audit is being built.
- Substantial effort has been placed on ensuring the leave accrual balance at year end is accurate where leave accrual was a qualifying finding in the Financial Statements at 30 June 2016.
- Due to the leave records only being available after 30 June 2017, Internal audit have only been able to conduct its review of leave accruals thereafter to determine accuracy and reliability of year end balances which figure will be adjusted in the annual financial statements.
- The Audit Committee have historically raised concerns in respect of the risks attributable to the Fresh Produce Market and in particular, the management of cash receipts. Recent internal audit reviews and tests in the Fresh Produce Market have shown that some internal controls have been put in place, however some areas for improvement remain. This represents a significant improvement in the management of the Fresh Produce Market.
- The Audit Committee have requested a meeting between the Auditor General and the Audit Committee only. This meeting should be scheduled at the Auditor General's earliest convenience to discuss relevant matters identified by the Office of the Auditor General.

2. Forensic Investigations

- The NMBM re-established the anti-fraud hotline in September 2016 which has received over 254 calls up to 30 June 2017 which related to:
 - Supply Chain,
 - Appointment irregularities
 - Nepotism
 - Work outside Municipal working hours / Conflict of interest
 - Mismanagement of Funds
 - Fraud / Corruption/Theft
 - Building irregularities
 - Unauthorised scarce skills
 - Dishonesty
 - Fraudulent advertisement
 - Overtimes irregularities
 - Maladministration
 - Theft
 - Unethical behaviour

- National Treasury are continuing with an external forensic investigation in respect of the IPTS. This investigation is on-going and as yet incomplete, where a final report thereon has not been concluded.
- The Audit Committee submitted their completed Fraud Risk Questionnaire for the year ended 30 June 2017 to the office of the Auditor General on 28 August 2017.

3. Risk Management

- The appointment of the Chief Risk Officer in October 2016, together with the appointment of the Risk Management Committee Chairperson has seen the Risk Management Unit of the Municipality continue to positively contribute to identifying high residual risks to be addressed by management.
- Two new risk specialists have been appointed to the Risk Management Unit who will add further capacity.
- Internal Audit have considered those high residual risks identified in the preparation of the annual audit plan 2017/2018. Future internal audit assurance reports will further assist Management through the implementation of those recommendations made against identified internal control weaknesses.
- Internal Audit also conducted a review of the Risk Management Unit during the 2016/2017 financial year and made recommendations for improvement in the functioning of the Unit.
- Previously appointed risk champions within the Municipality's Directorates have been re-appointed and registered for E-Learning. This will contribute positively to improved risk management capacity.
- All Directorates have considered and tabled their respective high residual risks.
- The Risk Management Unit of the NMBM will further assist the Mandela Bay Development Agency (MBDA) in identifying high residual risks. This is especially important with the MBDA having taken over the management of the Nelson Mandela Bay Stadium.
- In reviewing the current organisational structure, a significant gap exists between the current "As-Is" and "To-Be" capabilities.
- Although significant progress has been made in the services of the Risk Management Unit to the Municipality over the past year, capacity within the unit remains at a low level to deliver the required services to an institution the size of the Nelson Mandela Bay Municipality.

4. Information Technology Governance

- Per the 2016/17 Internal Audit plan, an IT user access review over the integrated scorecard system would have taken place. The integrated scorecard system will however be replaced by the new Enterprise Management System, as required to comply with mSCOA. The internal audit

review of the new Enterprise Management System has been included in the 2017/18 internal audit plan.

- In addition, an IT Governance Framework - Readiness Review, IT General Controls, Application Controls and User Access Review over Payroll and IT General Controls Review over the iForce Traffic Management System was conducted during the 2016/2017 financial year.

5. Financial Reporting

- Improved financial reporting is noted by the Audit Committee in respect of the timeous receipt of the draft financial statements allowing the Audit Committee to review the financial statements ahead of their submission to the Auditor General.
- The financial statements and certain working papers supporting the statements were further reviewed by Internal Audit.
- There has been noted improvement by Budget and Treasury in addressing high risk findings by Internal Audit and the Auditor General, with recommendations having been effectively implemented improving the control environment.
- Financial disclosures made by Management were complete in respect of GRAP and accurately reflect the Municipality's financial position, results of operations and long term commitments.
- The Audit Committee reviewed the accounting policies set out per the draft Annual Financial Statements with minor amendments being required. The accounting policies were found to be compliant with GRAP.

6. Performance Management

- The Audit Committee reviewed the performance management report for the year ending 30 June 2017.
- KPI's were considered to be relevant and appropriate, within the municipal mandate to enhance service delivery. KPI's are verifiable with targets being measurable. KPI's are generally well defined with targets being specific.
- New KPI's were considered and found to be relevant, enhancing service delivery.
- Over-performance was noted in two areas, where there was not a common understanding as to the methodology re: performance measurement counting. This matter has since been resolved.
- An improvement in the timing of the issuing of the performance management report to the Audit Committee as measured against the prior year has allowed the Audit Committee to carry out a thorough review of the report in advance of the report being issued to the Auditor General. This improvement is seen to be as a result of improved co-operation and submission of relevant reporting information between relevant Directorates and the Chief Operating Officer's office.

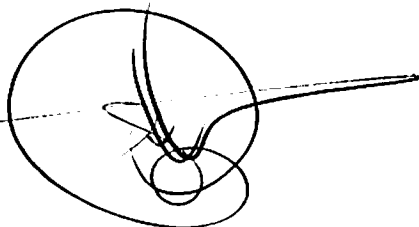
7. Effective Governance

- The Audit Committee scheduled two pre-year end meetings to review both the Annual Financial Statements and the Annual Performance report. The initial meeting, where all required information was available in advance allowed the committee to conduct a thorough review with a subsequent follow up meeting to ensure that recommendations and / or amendments had been considered and implemented. Other items on which further explanations were sought were effectively addressed at the second follow up meeting.
- Management should continue build an environment of ethical behavior, with visible discipline and accountability being actioned where necessary.
- The Audit Committee have not yet met the Executive Mayor. A meeting between the Audit Committee and the Executive Mayor should be scheduled as soon as possible.
- Internal legal capacity and the effective service delivery by the Legal Sub-Directorate within the NMBM should be considered a priority, allowing for less reliance on external legal service providers where substantial costs are being incurred.

8. Conclusion

- The Audit Committee notes an improvement in effective and efficient financial management and performance management within the Municipality. The control environment will continue to be strengthened where noted breakdowns in internal controls within identified high risk areas are addressed. The on-going improvement in the effectiveness of the Risk Committee Unit in assisting the Municipal Directorates to identify and address high residual risks will further reduce future irregular, fruitless and wasteful expenditure, and reduce exposure of the institution to possible fraud and error.

Yours sincerely,

A handwritten signature in black ink, consisting of a large circle with a vertical line through it and several loops and flourishes extending from the base of the circle.

Gregory Billson
Chairperson – Audit Committee

cc: City Manager
Executive Mayor
Executive Directors