



# MATATIELE

LOCAL MUNICIPALITY

## INTERNAL AUDIT CHARTER 2018/2019

**APPROVED BY COUNCIL: COUNCIL RESOLUTION NO: 527/29/10/2018**

**SIGNED BY ON BEHALF OF COUNCIL:**

**MUNICIPAL MANAGER**

**MAYOR**

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## **INTRODUCTION**

Internal audit charter is a formal written document that defines the purpose, authority, and responsibility of internal auditing.

The charter should:

- (a) Establish the internal audit activity's position within the organisation; must be allocated and report to the Accounting Office, Internal Audit manager to sit in General Management Meetings
- (b) Authorise access to records, personnel, and physical properties relevant to the performance of engagements; and
- (c) Define the scope of internal audit activities.

This charter therefore establishes the mandate conferred by the Matatiele Local Municipality Council on the Internal Audit unit.

## **2. MISSION**

Internal auditing is an independent, objective 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.

Assurance Services deal with evaluation of evidence to provide an independent assessment of governance, risk management and control processes. Auditors provide reasonable assurance at all times, not absolute assurance.

Consulting standards focus on activities beyond traditional assurance work, as requested by management, to help them meet the organizations objectives. The consulting services will be performed only upon written agreement between the internal audit of the municipality and the Council and or management of the municipality. Internal auditors will always maintain objectivity and not assume management responsibility.

## **3. PURPOSE**

- 3.1 The purpose of the internal audit is to provide an independent and thus objective review of the internal control systems within the local municipality.
- 3.2 Accordingly, the internal audit is responsible to both the Council and Executive Management, providing these structures with reasonable assurance regarding the effectiveness of the local municipality's corporate governance, risk management and the system of internal control.
- 3.3 This is achieved through bringing a systematic and a disciplined approach to the evaluation of the effectiveness of these governance prescriptions.

#### **4. LEGISLATION [MFMA Section 165, MFMA NT Circular 65 and IIA]**

Matatiele Local Municipality (“hereafter referred to as Matatiele”) is required to have an internal audit function in terms of section 165 (1) of the Municipal Finance Management Act no 56 of 2003 (“MFMA”). This Internal Audit Charter is crucial for strengthening the independence and objectivity of the internal audit function of the Local Municipality.

Internal Audit is responsible for conducting their work in accordance with the standards for the International Professional Practice Framework of Internal Auditing standards established by the Institute of Internal Auditors (IIA).

#### **5. AUTHORITY AND ACCESS**

The Internal Audit Department will remain independent of all line managers and report administratively to the Municipal Manager and functionally to the Audit Committee. The head of internal audit will administratively report to the municipal manager and will have free, ready and regular access to the executive mayor, the speaker of the council and the chairperson of the audit committee.

No restrictions should be placed on the scope of the Internal Audit work. Members of the internal audit function engaged on internal audit work are entitled to receive whatever information or explanations they consider necessary to fulfil their responsibilities.

Internal audit is authorised and mandated to:

- Allocate resources, determine the timing / frequency of the work, determine the scope of work, and apply the relevant techniques required to accomplish audit objectives.
- Internal auditor should report in all audit committee meetings. It is permissible that all reportable items by internal audit would have been presented to management beforehand and management offered the opportunity to comment on such findings and that such management comment including the method, timing and responsibility for addressing such audit findings and shall be an integral part of such final reports. The focus of Management comments shall be on providing solutions as against attempts to justify the status quo.
- In instances where internal audit has reason to believe that its independence has been or is likely to be compromised, it will have a right to refer such matters to the Audit Committee for review and resolution.

## 5. AUTHORITY AND ACCESS (Cont...)

Internal audit is not authorised to:

- Perform any operational duties for the municipality.
- Initiate or approve accounting transactions external to the internal audit department.
- Direct the activities of any employee in the organisation not employed by the internal auditing department, except to the extent that such employee(s) has / have been appropriately assigned to auditing teams or otherwise assisting internal auditors.

The existence of internal audit in no way diminishes the responsibility of Matatiele Local Municipality's management for implementing and maintaining effective systems of control, risk management and governance. Internal audit will not design or participate in control activities, as this would compromise its independence. However, internal audit can and will provide advice on the design and implementation of internal controls. Internal audit staff will have neither direct responsibility for, nor authority over, any of the activities that they audit.

## 6. RESPONSIBILITIES OF INTERNAL AUDIT UNIT

### 6.1 *STATUTORY RESPONSIBILITIES IN TERMS OF SECTION 165 OF THE MFMA*

**The internal audit unit must:**

- 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 audit plan and matters relating to:
  1. Internal audit;
  2. Internal controls;
  3. Accounting procedures and practices;
  4. Risk and risk based management;
  5. Performance management;
  6. Loss control
  7. Compliance with the MFMA, the annual Division of Revenue Act and any other applicable legislation
  8. Perform such other duties as may be assigned to it by the accounting officer.

## 6.2 *OTHER DUTIES AND RESPONSIBILITIES*

- Review directorates within the municipality at appropriate intervals to determine if they are efficiently and effectively carrying out their functions of planning, organising, directing and controlling in accordance with Councils instructions, policies and procedures.
- Determine the adequacy and effectiveness of the controls encompassing the Municipality's governance, operations and information systems.
- Review the reliability and integrity of financial information and the means used to identify measure and report such information.
- Review the established systems to ensure compliance with those policies, plans, procedures, laws and regulations that could have a significant impact on operations and reports, and determine whether the organisation is in compliance.
- Review the means of safeguarding assets and as appropriate, verify the existence of such assets.
- Appraise the economy and efficiency, with which resources are employed, identify opportunities to improve operating performance and recommend solutions to problems if appropriate.

### 6.2 *OTHER DUTIES AND RESPONSIBILITIES (Cont..)*

- Review operations and programs to ascertain whether results are congruent with established objectives and goals and whether the operations or programs are being carried out as planned.
- Coordinate activities with other internal and external providers of assurance and consulting services.
- Participate in the planning, design, development, implementation and operation of major computer-based systems to determine whether;
  - Adequate controls are incorporated in the system;
  - Thorough system testing is performed at appropriate stages;
  - System documentation is complete and accurate; and
  - The needs of user organisation are met.
- Review compliance with the council's guidelines for ethical business conduct and see that the highest standard of personal and council's performance is met.
- Submit annual engagement plans to the Audit Committee for review and approval.
- Provide adequate follow up to ensure corrective action is taken and that it is effective.

## 6.3 MSCOA AND AUDIT VALUE CHAIN

### 6.3.1 INTERNAL AUDIT, THE AUDIT COMMITTEE AND RISK MANAGEMENT

“A conversion to a new system is one of the highest risks that any organisation can face1.”

**Internal auditors:** should evaluate both the information technology (IT) and organisational aspects of the mSCOA system conversion projects. Auditing these conversions provides assurance to management and the municipal council that ‘all that can be done is being done’. The internal auditor's involvement and independent assessment of mSCOA project plans provides value that far outweighs the audit's costs.

Internal audit has an important role to play in ensuring good *m*SCOA project governance, including achieving *m*SCOA project goals and to create and maintain particular organisational values. It does so through the appropriate accountability and by evaluating processes that contribute to the achievement of these goals and values, specifically the communication of the goals and values and the processes used to monitor their achievement.

**Risk management:** is a key responsibility of management and the accounting officer (municipal manager). It is crucial that the municipality manages its *m*SCOA project risks as part of its normal risk management processes, including assigning clear responsibility for the management of *m*SCOA project risks. Internal auditors assist both management and the audit committee by examining, evaluating and reporting on the adequacy and effectiveness of the municipality's overall and particularly *m*SCOA project risk management process. Risk management is an essential part of effective *m*SCOA project governance and whilst it is a management responsibility, management can expect the audit committee to oversee and provide advice on the risk management of such a significant reform in the municipality. The audit committee needs to review:

- Whether management has a comprehensive risk management framework guiding the management of *m*SCOA project risks;
- Whether a sound and effective approach has been followed in developing the strategic risk management plan for the *m*SCOA project;
- The impact of the municipality's risk management framework on particularly the control environment of the *m*SCOA project; and
- The municipality's "*m*SCOA project" - fraud prevention plan to be satisfied that the municipality has appropriate processes and systems in place to capture, monitor and effectively investigate any fraudulent activities related to the project.

Management is responsible for ensuring the establishment of effective risk management in the municipality and in this case, also specifically for the *m*SCOA project. The approach followed provides a mechanism of formalising the responsibility and establishing accountability for management activities. For this project, it is crucial that either the established "Risk Committee" function or alternatively, the *m*SCOA steering committee oversee the *m*SCOA project risk management. These committee(s) efforts should identify further actions that may be needed to reduce *m*SCOA project risk to an acceptable level. National Treasury is in the process of developing an *m*SCOA position paper providing guidance to internal auditors of piloting and non-piloting municipalities on specific areas of importance in the context of a municipality's annual audit plan. The position paper will formally be communicated to all municipalities once it is finalised.

## **7. SCOPE**

### **7.1 *Compliance and regularity Audit***

Compliance Auditing is performed after the internal controls have been evaluated and is defined as a test of controls. The overall objective of this is to express an opinion - i.e. satisfactory, needs improvement, or unsatisfactory on the achievement of the control objectives of each significant system.

- Auditing of financial transactions which includes the evaluation of compliance with applicable laws, regulations, policies and instructions.
- Audit of the policy and propriety of administrative decisions taken within the municipality; and
- Reporting of any other matter arising from or relating to the audit that the auditor considers should be disclosed.

Internal Audit is aimed at promoting efficient, economical and effective management processes and evaluating the soundness, adequacy and effectiveness of internal controls by:

- Appraising the effective conduct of municipal operations;
- Reviewing the reliability and integrity of financial, operating and management information;

### **7.1 *Compliance and regularity Audit (Cont...)***

- Ascertaining the extent to which assets and departmental interests are being properly controlled and safeguarded from losses of any kind;
- Appraising the economy and efficiency with which financial, human and other resources are employed and
- Monitoring the accomplishment of established objectives and goals for programmes.

### **7.2 *Performance Auditing***

The promotion of economy, efficiency and effectiveness depends on adequate overall management arrangements for planning, budgeting, authorisation, control and evaluation of the use of resources. The responsibility of a performance audit is to confirm independently that measures do exist and are effective and to report to the management and the Audit Committee on these issues. In the course of an investigation into overall management arrangements in the municipality the following will receive attention:

- Systems planning, budgeting, authorisation, control and evaluation in respect of revenue, expenditure and the allocation of resources;
- The effect of decisions beyond the control of the municipality which have had an adverse influence on the municipality;
- Measures ensuring the proper management of all the resources of the municipality;



- Measures developed to derive benefit from economies of scale of expertise, especially in the provision of goods and services;
- Specific steps aimed at improving the economy, efficiency and effectiveness of the activities of the municipality;
- Proper assignment of responsibilities, powers and accountability;
- Measures to monitor results against predetermined objectives, to ensure that unacceptable performance is corrected timeously;
- Whether policy objectives were set and policy decisions taken with the necessary authority;
  
- The extent to which policy objectives were set and decisions taken on the basis of adequate, appropriate and reliable financial and other information and whether the critical underlying assumptions have been disclosed;
- If satisfactory arrangements for the consideration of alternative possibilities were made;
- Whether established policy goals and objectives as well as decisions on the implementation of policy are clearly defined and in line with the priorities of the Council; and whether they were taken with proper authority at the appropriate level;
- Whether conflict exists between the various policy goals or objectives, or between the methods chosen to implement them;

### **7.3 Information Technology Reviews**

A review of the Information Technology (IT) control to obtain an understanding of the control environment to support the audit risk assessment and to ensure that proper IT controls are in place.

Apart from the review referred to above it can also review specific computer and applications controls, control over changes in the computer systems, the methodology of systems development, internal controls and procedures, back-up and recovery procedures, disaster recovery plan and the physical control of the computer facilities.

Segregation of duties other than those enforced by manual procedures, like programmed procedures and passwords may be audited. Risk rating of all systems and functional areas as seen by management may be reviewed, and the management of these risks should be reported on.

### **7.4 Fraud Limitation**

The identification and prevention of fraud is clearly a management responsibility. Internal audit is well qualified to assist management to identify the main fraud risks facing the municipality and could assist management in designing appropriate controls to minimise the risks. However, in terms of standard 1210 – Internal auditors must have sufficient knowledge to evaluate the risk of fraud but is not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

### **7.5 Risk Management**

Internal Audit has to assist the Matatiele Local Municipality Council and Managers in identifying and evaluating the municipality's risk management processes to give an opinion on the adequacy and effectiveness of risk management and internal control systems.

Management should determine the role internal audit can play, but without taking ownership thereof or managing the process.

Internal audit will carry out risk based auditing, entailing a comprehensive risk assessment of the municipality, preparation of the resultant audit plan, execution thereof and reporting on the results of such work. The risk based auditing referred to above will entail a review of business risk, control risk as well as the financial risks Matatiele is exposed to.

The internal audit plan should be based on risk assessment as well as on issues highlighted by the audit committee and management. The risk assessment process should be of a continuous nature as to identify not only residual or existing but emerging risks and should be conducted formally at least annually and also as often as necessary. The risk assessment should be co-ordinated with the council's own assessment of risk.

## **8. RELATIONSHIP WITH EXTERNAL AUDITORS**

The Internal Audit department will co-ordinate their work with the External Auditors. The external auditors will be notified of the activities of internal audit in order to minimise duplication of audit effort. This will be accomplished by:

- Regular meetings between the Internal Audit Department and External Audit to discuss the annual internal and external audit plans;
- Access by the external auditors to the internal audit documentation;
- Exchange of management letters;
- Access to systems documentation.
- External audit being able to rely on the work of internal audit.

## **9. PLANNING, CONTROLLING, RECORDING AND REPORTING**

### **9.1 Internal audit plan**

Internal Audit will in consultation with management present an annual internal audit plan to the Audit Committee for approval. The plan shall set out the recommended scope of their work in the period.

The annual plan will be developed with reference to a long term strategic outlook for internal audit work (three-year plan), prepared in conjunction with management and approved by the Audit Committee, and should have regard to the plans of the municipality as a whole.

## 9.2 *Planning*

The primary purpose of internal audit planning includes:

- Determination of priorities in order to establish the most cost-effective means of achieving audit objectives
- Assist in the direction and control of audit work
- Help ensure that attention is devoted to practical aspects of internal audit work
- Help ensure that work is completed in accordance with predetermined targets.

The stages of internal audit planning include:

- Defining internal audit objectives
- Taking account of relevant changes in legislation and other factors
- Obtaining a comprehensive understanding of the system, structure and operations
- Identifying, evaluate and rank risks to which the municipality is exposed
- Taking account of the known strengths and weaknesses in the internal control system
- Taking account of management concerns and expectations
- Identifying audit areas by component and major systems
- Taking account of changes in structures or major systems
- Determining the type of audit;
- Taking account of the plans of external audit

Operational work plans should be prepared for each internal audit assignment, including:

- Objectives and scope of the audit
- Time budget and staff allocations
- Methods, procedures and reporting arrangements, including supervision and allocation of responsibilities

All internal audit plans should be sufficiently flexible to respond to changing priorities.

## 9.3 *Quality Control Mechanisms*

Control of the individual assignments is needed to ensure that internal audit objectives are achieved and work is performed effectively. This is facilitated by an established internal audit approach and standard documentation. The Internal Audit manager shall ensure that the necessary degree of control and supervision is exercised.

The Internal Audit manager shall establish arrangements to:

- Allocate internal assignments according to the level and proficiency of internal audit staff.
- Ensure that internal auditors clearly understand their responsibilities and internal audit objectives.
- Communicate the scope of work to be performed and agree the programme of work with each internal auditor

- Provide and document evidence of adequate supervision, review and guidance during the internal audit assignment
- Ensure that adequate working papers are prepared to support internal audit findings and conclusions

#### **9.4 Recording**

##### **Internal audit work shall be recorded.**

- The Internal Audit manager needs to be able to ensure that work delegated to staff has been properly performed. This will be done through reference to detailed working papers prepared by the internal audit staff that performed the work.
- Working papers provide, for future reference, evidence of work performed, details of problems encountered and conclusions drawn
- The preparation of working papers should encourage each internal auditor to adopt a methodical approach to his work
- The Internal Audit manager shall specify the required standard audit documentation and working papers and ensure those standards are maintained. Internal audit working papers should be sufficiently complete and detailed to enable an experienced internal auditor with no previous connection with the internal audit assignment to subsequently ascertain from them what work was performed to support the conclusions reached.

#### **9.5 Evaluation of the internal control system**

The main objectives of the internal control system are to:

- Ensure adherence to management policies and directives in order to achieve the objectives
- Safeguard assets
- Secure the relevance, reliability and integrity of information and as far as possible the completeness and accuracy of records
- Ensure compliance with statutory requirements.

When evaluating internal control systems Internal Audit should consider the effect which all the controls have on each other and or related systems. The stages of a systems audit include:

- Identifying the system parameters
- Determining the control objectives
- Identifying the expected controls to meet control objectives
- Reviewing the system against expected controls
- Appraising the controls designed into the system against control objectives
- Testing the operation of controls in practice
- Giving an opinion based on audit objectives as to whether the system provides an adequate basis for effective control and whether it is properly operated in practice.

## 9.6 Evidence

**Internal audit evidence is information obtained by an internal auditor which enables conclusions to be formed on which recommendations can be based.**

Internal Audit should determine what evidence will be necessary by exercising judgment in the light of the objectives of the internal audit assignment. This judgement will be influenced by the scope of the assignment, the significance of the matters under review, their relevance and the reliability of available evidence and the cost and time involved in obtaining it.

### 9.6.1 Collection and Assessment of Evidence

The collection and assessment of internal audit evidence should be reviewed to provide reasonable assurance that conclusions are soundly based and internal audit objectives achieved.

Internal Audit should obtain the evidence considered necessary for the achievement of the internal audit assignment objectives. This is influenced by the following:

- The level of assurance required
- The objectives and scope of the audit assignment
- The scale of activity under review and the degree of risk involved
- The cost/benefit involved in obtaining evidence
- The reliability of the evidence

### 9.6.2 Relevance and Reliability of Evidence

- The relevance of the internal audit evidence should be considered in relation to the objectives of the internal audit assignment.
- Reliable evidence can be achieved through the use of appropriate internal audit techniques which would normally be selected in advance, but which may be expanded or altered as necessary during, the internal audit assignment.
- In order to place reliance on evidence, the Internal Audit Department should be satisfied with its nature, extent, adequacy, consistency and relevance to the internal audit assignment and with the methods governing its collection.

## 9.7 The IIA Code of Ethics

The Code of Ethics was adopted by the Institute of Internal Auditors, with a purpose of promoting an ethical culture in the profession of internal auditing.

The Institute's Code of Ethics extends beyond the definition of internal auditing to include two essential components:

- Principles that are relevant to the profession and practice of internal auditing; and
- Rules of conduct that describe behaviour norms expected of internal auditors. These rules are an aid to interpreting the principles into practical applications and are

intended to guide the ethical conduct of internal auditors. The rules of conduct are defined into:

- ❖ Integrity;
- ❖ Objectivity;
- ❖ Confidentiality; and
- ❖ Competency

#### 9.8 **The Ten (10) Core Principles for the Professional Practice of Internal Auditing**

- Demonstrate integrity.
- Demonstrate competence and due professional care.
- Is objective and free from undue influence (independent).
- Aligns with the strategies, objectives, and risks of the organisation.
- Is appropriately positioned and adequately resourced.
- Demonstrates quality and continuous improvement.
- Communicates effectively.
- Provide risk-based assurance.
- Is insightful, proactive, and future-focused.
- Promotes organizational improvement.

#### 9.9 **Internal audit unit is 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;
- Obtain advice from the audit committee 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 internal audit function;
- Submit the internal audit charter to the audit committee for review and approval on an annual basis and as necessary.

#### 9.10 **Reporting**

The primary purposes of internal audit reports are to provide management with an opinion on the adequacy of the internal control system, and to inform management of significant audit findings, conclusions and recommendations.

The aim of every internal audit report should be:

- To prompt management to implement recommendations for change leading to improvement in performance and control,

- To provide a formal record of points arising from the internal audit assignment and, where appropriate, of agreements reached with management.

Reporting arrangements, including the format and distribution of internal audit reports, should be agreed with management. The Internal Audit manager should ensure that reports are sent to managers who have a direct responsibility for the unit being audited and who have the authority to take action on the internal audit recommendations. Internal audit reports are confidential documents and their distribution should therefore be restricted to those managers who need to know, the Audit Committee and the External Auditors.

The Internal Audit department should produce clear, constructive and concise written reports based on sufficient, relevant and reliable evidence, which:

- State the scope, purpose, extent and conclusions of the internal audit assignment
- Make recommendations which are appropriate and relevant, and which flow from the conclusions
- Acknowledge the actions taken, or proposed, by management

#### **9.10.1 Reporting**

The Internal Audit Department should prepare flash reports to alert management to the need to take control, or when there are reasonable grounds for suspicion of fraud or theft.

Consideration should also be given to reporting where there is a significant change in the scope of the internal audit assignment or where it is desirable to inform management of progress. Interim reporting should not diminish or eliminate the need for final reporting.

The Internal Audit manager should meet with management to discuss the audit findings during, and at the completion of fieldwork for each internal audit assignment and the formal written report should be presented to management as soon as possible thereafter.

Before issuing the final report, the Internal Audit should discuss the content with appropriate levels of management, and submit a draft report to them, for confirmation of factual accuracy.

If the Head of Internal Audit and management disagree about the factual content of the draft audit report, internal audit should review the situation, if reference should be made to this in the final report. No manager may alter the content of any report by the Internal Audit to the Audit Committee, but may furnish comment thereon on the agenda.

It is management's responsibility to ensure that proper consideration is given to internal audit reports. Internal Audit should ensure that appropriate arrangements are made to determine whether action has been taken on internal audit recommendations or that management has understood and assumed the risk of not taking such action.

## 10. INDEPENDENCE AND OBJECTIVITY

Independence of the Internal Audit Department will be ensured by:

- Internal audit will have full access at all times to any records, properties and resources relevant to the subjects under review.
- Have full and free access to the Chairperson of the Audit Committee.
- The Internal Audit function being free of any undue influences which could restrict, over-rule or otherwise affect the judgement as to the content of a report or in any way require the department to function under duress or which could affect the institution or conduct of an investigation.
- Respect, unqualified support and co-operation of both the Council and Management
  
- The appointment and dismissal of the internal audit Manager shall be with the concurrence of the audit committee.

## 11. CONCLUSION

It is management's responsibility to maintain the internal control system and to ensure that resources are properly applied in the manner and to the activities intended. This includes responsibility for the prevention and detection of fraud and other illegal acts.


The Municipal Manager is responsible for maintaining this Internal Audit Charter in the current state. Amendments of this Charter are subject to the approval by Council, after they have been reviewed by the Audit Committee annually.



**12. APPROVAL OF INTERNAL AUDIT CHARTER:**

  
\_\_\_\_\_  
**The Municipal Manager**

29/10/2018  
**Date**

  
\_\_\_\_\_  
**Chairperson of Audit Committee**

29/10/2018  
**Date**

  
**Approved by Mayor**

29/10/2018  
**Date**