



The Relationship between Audit Committees and Governing Bodies

(This guidance paper is applicable to Local Government, Departments and Public Entities)

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1. Introduction

The purpose of this paper is to highlight the importance of an effective relationship between the Audit Committee and Governing Body, and to provide practical guidelines on improving this relationship.

Each function within the governance structure of organs of state has its individual role to play, however there needs to be co-operation and collaboration between these functions in pursuit of a common goal, i.e. fulfilling the overall objectives. Effective working relationships that value all contributions will foster a team approach, ensure effective fulfilment of responsibilities and boost morale.

The roles to be played by the Governing Body and Audit Committee have been legislated in the relevant legislation. The Audit Committee has been legislated in to provide independent advice and oversight in terms of financial and non-financial matters in order to improve the effective functioning of organs of state. In addition, many audit findings can be prevented or mitigated through proper oversight by the Audit Committee.

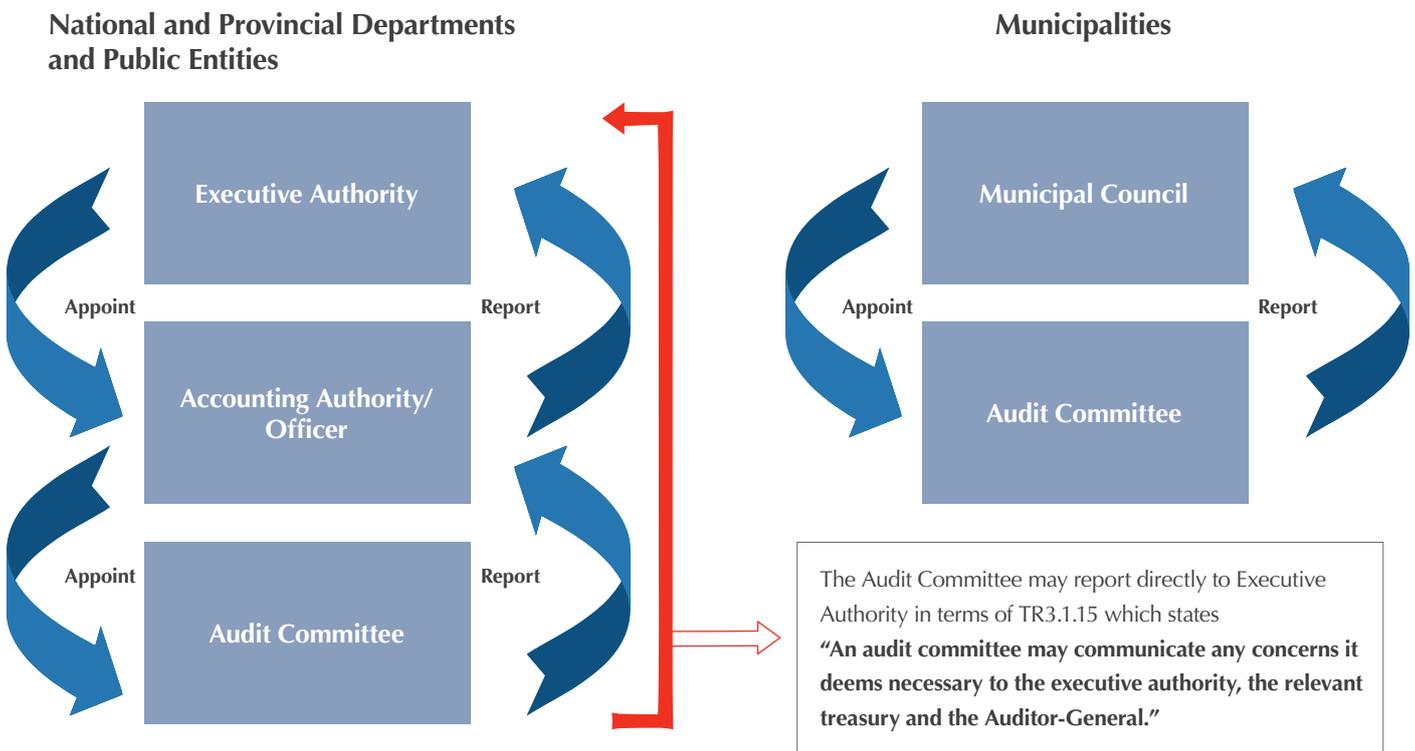
2. The Role of the Governing Body

The role of a Governing Body is to oversee an entity's strategic direction, operations, and accountability.

The Governing Body for the following institutions are as follows:

- Municipality – municipal council
- Municipal entity – municipal council
- National and Provincial department – executive authority
- Public Entities – executive authority

The reporting structures that exist at National Departments, Provincial Departments and Public Entities, and municipalities are as follows:



3. The role of Audit Committee

The Audit Committee is a key contributor to good governance. It plays a crucial role in assisting the relevant Governing Body in discharging its responsibilities in overseeing financial and performance management, compliance with legal and other regulatory requirements and internal controls.

Typically the responsibilities of a public sector Audit Committee includes overseeing matters related to:

- financial management
- performance management
- external audit
- internal audit
- risk management
- internal control
- IT governance
- compliance with laws
- combined assurance
- other regulatory requirements

4. Interactions between Governing Bodies and Audit Committees

Key concerns identified by the Audit Committee that affects the effective functioning of an organ of state should be escalated to the Governing Body.

² In this paper, the term relevant governing body should be read to include Board, Accounting Authority or Council as applicable to the relevant public sector entity.

The following table serves as a guideline of issues that should be escalated by the Audit Committee to the Governing Body and is not an exhaustive list:

Area	Issue	Reporting structure for Local Government	Reporting structure for National and Provincial Departments and Public Entities
Risk and control	Summary of key risks facing the organ of state and how these are being addressed.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. Escalate to Executive Authority where the Accounting Officer/ Accounting Authority is not addressing significant risks.
	Effectiveness of internal controls and any additional measures that should be implemented to address identified risks.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should escalate to the Executive Authority where the Accounting Officer/Authority does not implement the audit committee's recommendations on additional measures that should be implemented to address risks identified.
Assurance	Significant external audit findings, recommendations and updated status thereof.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should escalate to the Executive Authority where the Accounting Officer/Accounting Authority does not implement recommendations to resolve significant external audit findings.
	Significant internal audit findings, recommendations and updated status thereof.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should escalate to the Executive Authority where the Accounting Officer/Accounting Authority does not implement recommendations to resolve significant external audit findings.
Finance	Recommendation of draft financial statements for approval.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority.
	The Audit Committee's view on the financial position of the organ of state.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should escalate to the Executive Authority where the audit committee raises significant issues on the financial position of the organ of state and the Accounting Officer/Accounting Authority does not implement controls to resolve it.
Compliance	Any areas of non-compliance with relevant legislation.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should escalate to the Executive Authority where the Accounting Officer/Accounting Authority does not implement controls to resolve significant non-compliance findings.
	Audit committee's findings and recommendations in line with service delivery and budget implementation plan.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should escalate to the Executive Authority where the Accounting Officer/Accounting Authority does not implement recommendations of the audit committee on significant findings on service delivery and budget implementation.
General	Results of any Audit Committee evaluations that have been conducted.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority.
	Details of meetings and the number of meetings attended by each member of the Audit Committee.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority.
	Progress with any specific investigations delegated to the Audit Committee and their outcomes.	Report to municipal council.	Report to Accounting Officer/ Accounting Authority. The Audit Committee should report all outcomes of investigations to the Executive Authority.

5. Challenges affecting the interaction between the Audit Committees and Governing Bodies

Challenge 1: Role Clarity

The manner in which some public sector entities are structured makes this a specific challenge. For example, in the case of public entities, the Accounting Authority is seen as the board; however, the minister is involved in the appointment of the audit committee with the board. This appointment process may create some uncertainty as to direct reporting lines; however, there should be reporting to both parties.

Recommendation

In this respect, Audit Committees need to be aware of the following:

- Their reporting line is directly to the relevant Governing Body.
- There are no reporting lines to management. Management needs to report to the audit committee regarding financial and performance management and internal controls, allowing the committee to determine the adequacy of the design of the internal controls and their effective operation throughout the reporting period.
- The Audit Committee's role and level in the organisation is that of an independent oversight body.
- Audit Committees should provide feedback to the relevant Governing Body after each Audit Committee meeting, which results in the escalation of significant issues.
- Audit Committees should meet with the minister (Executive Authority) at least annually to discuss governance matters.

The Audit Committee should engage with the executive authority to report matters that are not adequately dealt with to the committee's satisfaction. Interactions with the national or provincial treasury and/or oversight structures such as portfolio committees are encouraged.

Challenge 2: Independence

The independence of the Audit Committee may be impaired due to previous/current relationships of Audit Committee members or the Audit Committee as a whole and political standing, among other factors.

Recommendation

Measures should be in place to assess independence of Audit Committee members prior to appointment. Their independence should also be assessed on an ongoing basis throughout their term of office. Declarations of interest should be completed by Audit Committee members at every meeting.

6. Conclusion

Proper communication channels established between the Governing Bodies and Audit Committees will assist the Governing Body to effectively discharge its responsibilities in overseeing financial and performance management, compliance with legal and other regulatory requirements and internal controls.

7. Definitions

Definition	Source
Accounting Authority: “means a body or person mentioned in section 49 of the PFMA”	Public Finance Management Act No. 1 of 1999
Accounting Officer: “means a person mentioned in section 36 of the PFMA”	Public Finance Management Act No. 1 of 1999
Executive Authority: “(a) in relation to a national department, means the Cabinet member who is accountable to Parliament for that department; (b) in relation to a provincial department, means the member of the Executive Council of a province who is accountable to the provincial legislature for that department; (c) in relation to a national public entity, means the Cabinet member who is accountable to Parliament for that public entity or in whose portfolio it falls; and (d) in relation to a provincial public entity, means the member of the provincial Executive Council who is accountable to the provincial legislature for that public entity or in whose portfolio it falls.”	Public Finance Management Act No. 1 of 1999
Governing Body: “the person(s) or group with primary responsibility for overseeing an entity’s strategic direction, operations, and accountability.”	International Framework: Good Governance in the Public sector
Municipal Council: “means the council of a municipality referred to in section 18 of the Municipal Structures Act.”	Local Government: Municipal Finance Management Act, No. 56 of 2003
Organ of State: “means— (a) any department of state or administration in the national, provincial or local sphere of government; or (b) any other functionary or institution— (i) exercising a power or performing a function in terms of the Constitution or a provincial constitution; or (ii) exercising a public power or performing a public function in terms of any legislation, but does not include a court or a judicial officer;”	Constitution of the Republic of South Africa, 1996

8. References

- Constitution of the Republic of South Africa, 1996
- Local Government: Municipal Finance Management Act, No. 56 of 2003
- Public Finance Management Act No. 1 of 1999
- Challenges facing public sector audit committee *published by Public Sector Audit Committee*
- International Framework: Good Governance in the *Public Sector published by IFAC and CIPFA*

Annexure A: Prevailing legislations affecting the audit committee

In South Africa the following legislations are applicable to public sector audit committees:

- The Public Finance Management Act (Act No. 1 of 1999) (PFMA) makes it compulsory for all national or provincial public sector organisations to establish an (or share an established) audit committee.
- The Municipal Finance Management Act (Act No. 56 of 2003) (MFMA), applicable to local government, makes it compulsory to establish an (or share an established) audit committee.
- The Companies Act (Act No. 71 of 2008) for public entities that are registered as companies.

In South Africa the following best practice is also applicable:

- King IV Report on Corporate Governance in South Africa 2016

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