



GMA INTERNAL AUDIT

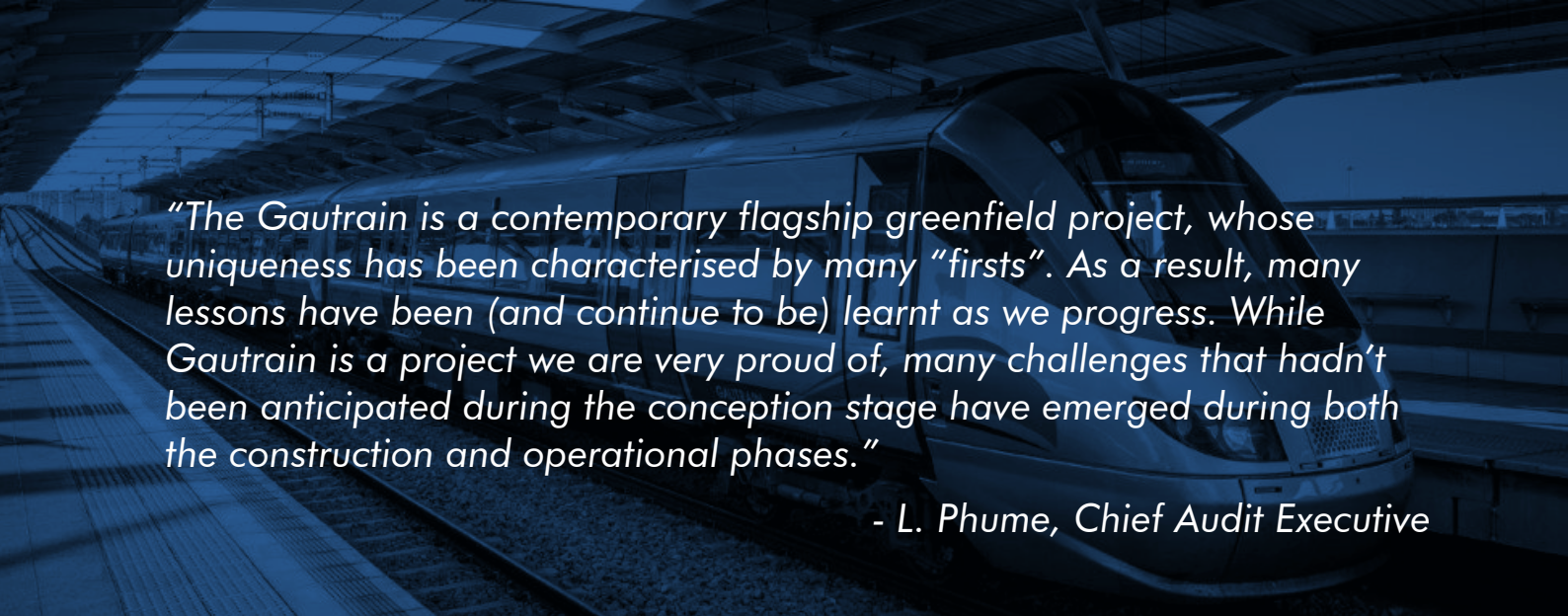
OUR AUDITING TRAJECTORY

From Construction to Operational Phase



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“The Gautrain is a contemporary flagship greenfield project, whose uniqueness has been characterised by many “firsts”. As a result, many lessons have been (and continue to be) learnt as we progress. While Gautrain is a project we are very proud of, many challenges that hadn’t been anticipated during the conception stage have emerged during both the construction and operational phases.”

- L. Phume, Chief Audit Executive

These challenges were found within the entire business value-chain, as well as within each business unit, and required the Gautrain Management Agency (GMA) to think on its feet. It’s therefore critically important that we as the GMA record all the lessons we have learnt, so that we can manage future similar PPP projects better. It is for this reason that a case study focusing on the internal audit journey has been developed. Also, because of the unique position that the Internal Audit unit holds in the business, an environmental scan of the unit has been outlined in order to provide context and ease of reference. This case study concludes with a reflective outlook for the successful management of large public infrastructure projects in future, particularly within the context of combined assurance in the public service.

BACKGROUND

As an agency reporting under the Gauteng Department of Public Transport, Roads and Works (GPTRW), the GMA started as a project office before it was formally established as a Schedule 3C (of PFMA) public entity, through the GMA Act, Act No. 5 of 2006.

Consistent with the requirements of Schedule 3C, the GMA has to comply with all the relevant provisions of the Public Finance

Management Act (Act 1 of 1999) (PFMA). With specific reference to internal auditing, section 51 (1) (a) (ii) of the PFMA states that:

“An accounting authority for a public entity must ensure that the public entity has and maintains a system of internal audit under the control and direction of an audit committee of the Board complying with and operating in accordance with regulations and instructions prescribed in terms of sections 76 and 77...”.

The intention of the PFMA is that the Board is ultimately responsible for overseeing the establishment of effective

internal controls, in order to provide reasonable assurance that the GMA’s financial and operational objectives are achieved. Executing this

responsibility includes the establishment of an Internal Audit in accordance with a Board-approved Charter.





CONSTRUCTION PERIOD

As a Project Office reporting to the MEC for DORT, GMA's books were audited by the Auditor-General (AG), as a vote (a unit or arm) of the DORT.

Internal Audit activity within the whole of the Gauteng Provincial Government (GPG) is centralised within the department of Finance. Before that it was under the control of the Gauteng Shared Services Centre (GSSC) and was known as GAS (Gauteng Audit Services). GAS provides internal auditing functions for DORT and other departments within the province. By extension, Gautrain Project Office was on the radar screen of GAS.

When auditing the books of DORT from 1998 to 2011, the AG expressed satisfaction around processes and controls being used to dispense Project funds. In essence, the AG certified that these controls and processes were designed to safeguard financial anomalies and were actually working as they were intended to. This expression of confidence on the controls within the Project Office by the AG was a stamp of approval that the books were clean.

OPERATIONAL PERIOD

Establishing the internal Audit and Finding Resources

Before the establishment of the in-house Internal Audit Unit (as it currently exists), the function was outsourced to Grant Thornton – an accounting and auditing firm. At the end of 2010 the Chief Audit Executive (CAE) was appointed to establish an in-house Internal Audit Unit, as envisaged in the PFMA.

Although the GMA was still very small in terms of number of staff, the Board of Directors (Board) as well as the Board's Audit and Risk Committee (ARC) were in place. Conforming with the International Standards for Professional Practice of Internal Auditing (the Standards), Internal Audit reported to the latter committee functionally and at the same time, reported administratively to the CEO. This dual reporting protocol was established to safeguard the independence of Internal Audit, as laid down in the PFMA and the Standards. Internal Audit tabled its first Charter (founding policy) to the Board for approval in

March 2011. This provided for the operational principles, roles and responsibilities, strategic direction, mission and vision of the Unit.

At the same time, Internal Audit submitted its three-year Rolling Risk-Based Strategic Plan for approval to the ARC. This plan covered the period 2011-14 (inclusive of the 2011-12 Operational Plan). Simultaneously, while embarking on a recruitment process for this new unit, the CAE prepared other frameworks such as Internal Audit Methodology and working papers (templates).

The recruitment process yielded two candidates to assist the CAE in executing the audit plan. These included a manager in charge of corporate and finance audits, and a manager responsible for technical and ICT audits. The unit has since added two more members who are specialists in these sub-units. The growth of the unit was necessary because of the expansion of the scope of work, in response to the operational challenges brought about by the growth of GMA itself.



Key Features of an Enabling Environment

- 1 Board Support
- 2 Management Support
- 3 Adequate Resources
- 4 Promote Independence
- 5 Code of Ethics
- 6 Good Relationship with Auditor-General
- 7 Risk Management
- 8 Fraud
- 9 Compliance
- 10 Internal Controls
- 11 Governance
- 12 Quality Assurance and Improvement Program
- 13 Combined Assurance

Internal Audit Approach

Internal Audit provides assurance and consulting services to the GMA in accordance with the Standards and the Code of Ethics, as issued by the Institute of Internal Auditors (IIA).

In general, internal auditors have three roles:

- ① Auditing
- ② Advisory
- ③ Consulting services to the GMA

The Unit's planning process is anchored on the GMA's risk profile and covers two spectrums:

- ① Three-year rolling internal audit strategic plan
- ② One-year operational plan

The two plans take into account the GMA strategy and are endorsed by management before they're submitted to the ARC for approval.

Overall, the plans cover auditable areas for a given financial year (or years). They also include the scope and any risks that threaten the achievement of GMA goals. Equally important, Internal Audit needs to be responsive to the complex and dynamic environments within which GMA operates. This should form an integral part of the planning process in order to ensure relevance and sustainable success.

Internal Audit Reports

During the operational period, Internal Audit reviews all

activities within the GMA, including transactions with the Provincial Support Team (PST). Internal Audit performs follow up reviews in terms of findings raised by the AG. Internal Audit also assesses the reliability of the Key Control Dashboard – an AG measurement tool designed to evaluate management's leadership, financial controls and operational efficiency.

All these reviews are reported to the respective senior executive managers and the CEO. The audit report includes findings and recommendations for actions to control weaknesses. On a quarterly basis, Internal Audit reports to MANCO and the ARC.

ENVIRONMENTAL SCAN

Internal Audit occupies a unique position within GMA. In terms of its mandate, it's required to adopt a helicopter approach when conducting its work, meaning that it must objectively and independently execute its Board-sanctioned mandate. Because of this, key features of an enabling environment are:

Board Support

Internal Audit is sometimes described as 'the eyes and ears' of the Board. It achieves this by providing the Board with independent assurance that the strategic goals are being pursued with the required controls and effective risk management processes in place.

Internal Audit submits quarterly consolidated reports to ARC which highlight:

- ① Progress against approved Annual Internal Audit Plan
- ② Summary findings of audit reports issued
- ③ Progress on implementation of internal audit agreed corrective actions
- ④ Internal Audit training and resource management

This means that for Internal Audit to thrive, it needs the utmost support from the Board.

Management Support

There is no doubt that one of the key outcomes of the Internal Audit being established is to make management “look good”. An analogy to demonstrate this is that Internal Audit’s role towards management is to clean the house before visitors arrive. By ‘visitors’ we mean entities such as the AG and other regulatory bodies whose purpose might be to find fault. So if Internal Audit cleaned up before their arrival, management would have been forewarned about the weaknesses within the processes and would have employed corrective actions at the right time.

In the case of the GMA, 90% of AG’s findings had been highlighted by Internal Audit way before the AG identified them. By the time the AG raised the findings, management would be halfway towards resolving these matters.

It is through this approach (together with management controls) that GMA has managed to obtain clean audit opinion for four successive years. In a sense, this makes management “look good” in the eyes of all the stakeholders.

Adequate Resources

Internal Audit needs tools of the trade to effectively execute their duties. Resources range from personnel to equipment and continuous training. Internal Audit competes with other business units for scarce resources but, when it receives its equitable share, it goes a long way to promoting a value-adding assurance partner.

Promote Independence

As advocated by the auditing Standards, Internal Audit should be independent from the work that they audit. This principle is embedded in the auditing profession and should be guarded jealously so that Internal Audit remains objective and functional. The rationale is that Internal Audit cannot be a referee and a player at the same time. Temptations to use Internal Audit for operational duties should therefore be discouraged.

Code of Ethics

Like any other professional function, Internal Audit adheres to the Internal Institute of Auditors (IIA) Code of Ethics.



This code is made up of fundamental principles underpinning basic requirements for the professional practice of internal auditing, upon which audit practitioners’ effectiveness is evaluated. The Code also helps to create a cohesive understanding of the ethic boundaries around Internal Audit Unit in terms of its contribution toward attaining GMA strategic goals. In addition, through Code of Ethics, GMA Internal Auditors pledge to promote good ethical culture, professional integrity and protection of the entity’s reputation.

Good Relationship with Auditor-General

The AG is a constitutional (chapter 9) institution mandated to express an opinion on the books of all public sector entities. The AG’s opinion matters and carries significant weight in terms of running the affairs of GMA. Adverse audit opinion is often followed by dire consequences for the organisation. Internal Audit

helps the organisation to have a soft landing in respect of the opinion given by the AG. As mentioned previously, Internal Audit would have cleaned up the house before AG lands, and when he arrives the house would be clean and so would be his opinion of the house.

Risk Management

Internal Audit works hand-in-hand with Risk Management unit. Internal Audit's plan is based on risks identified by management – hence the phrase Risk-based Internal Audit Plan. It's therefore in the interest of Internal Audit and management that the risk management processes adopted by the entity are adequate and effective. Internal Audit reviews the work of Risk Management to ensure that risk processes and the risk registers cover critical risks that may deter management from achieving its objectives. The results of the audit review help management to enhance the risk management regime within the entity. In summary, as is the case with respect to Corporate Governance,

Internal Audit is both a function (something required to perform their duty) and a functionary inherent to risk management.

Fraud

While it is not its primary duty to prevent and detect fraud, Standards charge Internal Auditors to be alert to the red flags that might give rise to fraud. They're also required to report these to the relevant authorities when they've been detected. The Standards go even further to state that Internal Auditors should satisfy themselves that the risk of fraud has been sufficiently mitigated by management and that there are fraud prevention systems in place. So, Internal Audit has a duty to provide assurance to management and the Board on the adequacy and effectiveness of controls that have been designed to prevent, detect and mitigate the risk of fraud.

Compliance

No audit will be complete without the expression on

the adequacy or compliance to rules, regulations, laws, policies, procedures, standards and other requirements. In this way, Internal Audit promotes adhering to compliance.

Internal Controls

Though the establishment of Internal Audit is in itself an exercise in control, the primary role of internal auditors is to review and evaluate the adequacy, efficiency and effectiveness of internal controls. Internal Audit therefore plays a huge role in promoting the maintenance of robust internal controls within the organisation and ensures that GMA manages the risk of control erosion down to an acceptable level.

The controls subject to review are:

- ① the information systems environment
- ② the reliability and integrity of financial and operational information
- ③ safeguarding of assets
- ④ compliance with laws, regulations and controls

Governance

Internal Audit is a product of corporate governance. It has been established under the Board charter and its stewardship has been delegated to the ARC of the Board. In the case of GMA, it is also a product of statutes like the PFMA. However, Internal Audit has a duty





to review the application and adequacy of governance processes within the organisation.

Internal Audit assists the Board and its committees by independently assessing the effectiveness and providing assurance on the organization's system of internal controls as well as compliance with laws, rules, regulations, policies and procedures.

Quality Assurance and Improvement Program

Internal Audit maintains a quality assurance and improvement program that covers all aspects of their unit. The program includes an evaluation of the Internal Audit Unit's conformance with the definition of Internal Auditing and the Standards, plus an evaluation of whether internal auditors apply the Code of Ethics.

The program also assesses the efficiency of the Internal Audit Unit and identifies opportunities to improve. The CAE communicates to senior management and the Board on the Internal Audit Unit's quality assurance and improvement program, including results of ongoing internal assessments and external assessments conducted at least every five years.

Combined Assurance

According to the Standards, the CAE should share information and coordinate activities with other internal and external providers of assurance to ensure proper coverage and minimize duplication of efforts. Internal Audit spearheads and coordinates the GMA's Combined Assurance activities. This is in line with corporate governance principles that require the ARC to "ensure that a Combined Assurance

Framework is applied to provide a coordinated approach to all assurance activities," says Chief Internal Audit Officer Livhu Phume.

OVERALL LESSONS LEARNT

One of the key objectives of writing this case study was to record the lessons learnt, to help GMA employees and other stakeholders make informed decisions in the future. All lessons listed here were learnt from the challenges we encountered while establishing a fully-fledged, independent and objective Internal Audit Unit within GMA. Each lesson is accompanied by suggested solutions for the benefit of those who will come after us.

Lesson 1: Maturity is Key

GMA has matured in terms of its attitude towards audit in general and internal audit in particular. This maturity is informed by the understanding that auditing is not there to punish or catch people out. Rather, it is a tool that helps management and the Board to "look good". For example, the fact that for four successive years the GMA has received clean audit reports from the AG (and not qualified audit opinion), can attest to that.

Solution:

- Get management buy-in.
- Use Internal Audit as a training ground for business unit managers.

Lesson 2: Requisite Skills

One of the challenges in the field of auditing is to attract suitably qualified and skilled audit practitioners. The challenge comes in the form of scarcity of personnel, as well as unaffordability for those who are available. We're pleased to report that the GMA has managed to overcome this challenge and we're now working with a dedicated and dynamic team of auditors.

However, the challenge that remains is to retain the current staff within GMA, as competition is stiff in the market place.

Solution:

- Establish a competitive reward and retention policy.
- Create a supportive team environment.
- Learn from mistakes and leverage these experiences.

Lesson 3: PPP Architecture

Another challenge is imposed by the nature of PPP architecture, which is restrictive when it comes to audit access to the concessionaire, when compared to ordinary corporates. It's a challenge because auditors by their nature are used to having unfettered access to information, systems, processes and personnel. Any restrictions therefore pose a challenge.

Solution:

- Extend the powers of the auditors provided for in

section 92 of the CA, which states that GMA could audit the concessionaire if there is a justifiable cause.

Lesson 4: Enterprise Risk Management (ERM)

The Standards require internal auditors to prepare a risk-based plan for approval by the ARC before the commencement of audit reviews. GMA was slow in embedding the risk management processes within its structures. As a result, Internal Audit struggled to prepare a plan generically based on risks that were identified and assessed by management. The Risk Management office has not been stable due to unforeseen staff turnover within the business unit. The instability poses a huge challenge in the smooth planning within the Internal Audit Unit.

Solution:

- Stabilise the Risk Management office.
- Embed ERM within process owners.
- ERM should be compulsory KPIs.

CONCLUSION

The benefits of having Internal Audit within GMA have been revealed inter alia through clean audit opinion from the AG.

This clearly shows that once management embraces Internal Audit and collaborates with it throughout the business value-chain, the results are immensely positive.



Lessons Learnt

Maturity is Key



Requisite Skills



PPP Architecture



Enterprise Risk Management (ERM)





AG reports are testimony to good corporate governance, which is a product of ethical leadership, integrity of financial and operational information, effectiveness and efficiency of controls, and compliance to rules and regulations. As a partner, Internal Audit assists the Board and management in achieving all of these key performance areas.

Furthermore, AG reports also illustrate the level and extent of service delivery and achievement of goals. This bodes well for the future of PPPs, whose success will rely heavily on the lessons learnt from the likes of GMA.

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