

# Internal Controls Underpinning Audit Outcomes in South African Municipalities

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**Abstract:** The internal control is defined as a process designed to provide assurance regarding the achievement of the entity's objectives through the coordinated efforts of everyone within the entity. This paper relied on Auditor-General of South Africa (AGSA) reports to establish the internal controls underpinning the audit outcomes in South African municipalities. Therefore, a qualitative research design using document analysis was implemented to achieve the paper's objectives. Data was collected through secondary data available in the public domain. The criterion sampling method was used for metropolitan municipalities whilst a simple random sampling method was used for district and local municipalities. The basic internal controls identified by the AGSA were examined and from these, five basic categories of internal control were identified. The findings revealed that internal controls are essential in achieving positive and clean audit outcomes. The paper recommends that the municipal leadership should attain adequate training to ensure that instability and under-performance of employees could be timely addressed. Furthermore, financial management risk can be reduced through implementation and managing internal control systems and monitoring by relevant assurance providers such as internal audit functions.

**Keywords:** Content analysis, Internal controls, Leadership, Metropolitan, Municipalities

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## 1. Introduction

Internal controls became important in organisations both private and public, that management is increasingly expected to submit an assessment of the efficiency and effectiveness of internal controls to the audit committee, especially as it relates to the accuracy and reliability of financial statements. Similarly, regulators are expected to improve the quality of financial reporting and therefore, enhance investor confidence (Calderon, Wang & Conrad, 2012:20). In addition, to ensure compliance with implemented legislation such as the Sarbanes – Oxley Act (SOX) many more organisations are assessing, testing and recording their internal controls for the purpose of financial reporting and disclosure. Other companies have recognised that effective internal controls are a necessity for long-term business continuity, therefore, they have joined in to comply with SOX although they are not required to do so (McNally, 2013:1).

Corporate scandals in South Africa, such as those that took place at Fidentia, a Financial Asset Management company, are an example of weak internal controls and management's lack of commitment to strengthen them (Gabrini, 2013:39). More recently,

the Venda Building Society (VBS) mutual bank collapse, known as the "bank heist", saw investors losing R2.3bn. According to Business Day (2018), only 33 out of 257 municipalities received a clean audit opinion in 2017, however, the municipal audit outcome report of 2016 put the number at 48. It has been revealed that 14 municipalities fell victim to this VBS scandal, and collectively lost about R1.2bn, which had been illegally deposited with the bank. According to Business Day (2018), these deposits were allowed by municipal finance officers, therefore demonstrating a lack of controls and accountability in many local administrations.

In South Africa, "the King Reports on Corporate Governance (1994, 2002, 2009, 2016), set out the code of corporate governance practice" (IoD, 2016). The King IV report defines corporate governance as "an exercise of ethical and effective leadership by the governing body towards the achievement of the four governance outcomes, namely, ethical culture, good performance, effective control and legitimacy" (IoD, 2016:7). It is evident that corporate misconducts are not only related to corporate entities but are equally applicable to public sector entities and municipalities.

In South African local municipalities, obtaining an unqualified audit opinion remains a challenge (Shiceka, 2009:1; AGSA, 2016:59). The AGSA's audit report's overall problem is the mismanagement of tax-payers' money (Ngoepe, 2012). For that reason, the government is required to move towards higher levels of transparency, thus demonstrating accountability in the use of tax-payers' money and efficiency in delivering services to their designated communities. Therefore, the internal controls are undoubtedly crucial for any municipality and if they are properly designed and implemented the municipality will always obtain positive audit outcomes. It is, therefore, important to establish the internal controls that are underpinning audit outcomes in South African municipalities. This paper seeks to analyse the specific internal controls required at municipalities in South Africa to assist the municipalities in obtaining positive audit outcomes. The three types of municipalities in South Africa, namely the metropolitan, district and local municipalities will be examined. The 2014 OCA deadline for 'clean' audits was missed by more than 90% of municipalities in South Africa (Stone, 2014). According to AGSA (2016:7) a lack of adequate controls negatively impacted audit outcomes. Despite many municipalities struggling to obtain 'clean' audits, some consistently improve on or maintain 'clean' audit outcomes. According to AGSA (2016: 52), the most prominent reason for unclean audit outcomes is due to poor control environments.

Research has found that companies which provide low-quality financial information is due to a weak internal control system (Ashbaugh-Skaife, Collins, Kinney & LaFond, 2008:247). In the municipal context in South Africa, it is therefore imperative to understand the types of controls relative to clean audit versus unclean audit. This research was conducted to generate an understanding of internal controls and how they impact audit outcomes.

This paper was guided by the following key research objectives: (i) to gain an understanding of the concept of internal control, (ii) to analyse selected municipalities' audit outcomes "clean versus unclean", in order to obtain an understanding of the type of internal controls which are prevalent to the two extremes of 'audit outcomes'. The key research question was: Which internal controls underpin clean audits compared to those with unclean audits?

## **2. Literature Review**

This section explores the history of internal controls from when they were first recognised and defined, until their contemporary use. The history and development of internal controls is important as it reveals the evolution of internal controls from ancient history to more contemporary developments.

### **2.1 Brief History of Internal Controls**

Stone (1969, as cited in Lee 1971:151), stated that "the first signs of internal controls can be found in the records of the early Mesopotamian civilization – the Sumerian – around 3600 to 3200 B.C." For example, they made use of stone tablets to record commercial transactions. Stone (1969:284) further explains that summaries would be prepared by scribes independent of those who provided the original payment list. Therefore, one can conclude that management of the time clearly had an idea of the accounting controls now known as segregation of duties. To substantiate this point, there are documents with evidence of internal control existence during that period which reveal dots, tiny marks and ticks and circles alongside the different figures, this proves that internal checks had been performed (Stone, 1969:284).

Moreover, Brown (1905: 21) noted that the Treasury of the Egyptian Pharaohs did not allow any movement of receipts or payments without a written order, and that the records of one official were checked by another. In the ancient Egyptian era, the use of money was unknown; therefore, receipts and payments were made in kind in the form of oxen, corn, or fabric. The Treasury itself consisted of farms and warehouses to store any items that were received as payments (Brown, 1905:21). In addition, the pharaohs central finance department used internal controls in a manner that when corn was received at the storehouses, the filling process was done under the supervision of an overseer and was thereafter noted down. Another scribe stationed at the roof of the storehouse where the corn sacks were delivered and emptied, recorded the number of sacks received.

To strengthen this view, the article based on historical dates in accounting by the American Accounting Association (1954:486) attests to the existence of internal controls dating as far back as 2000 BC, when the Egyptian treasurer's activities in collecting

grain were checked by a scribe. The controls used by the Egyptian pharaohs were meant to reduce the likelihood of fraud. According to Sampson (1999), authorisation and approval are control activities that mitigate the risk of inappropriate transactions, thus serving as a fraud deterrent and enforcing segregation of duties. It is evident that internal controls existed in ancient history, although they were only recognised and defined as the years progressed.

In the latter part of the twentieth century, internal controls practices changed (Page & Spira, 2004:9), influenced by the introduction of new technology and changes in audit approach. A well-known definition of an internal control activity before technological advancement was that the person responsible for opening incoming mail payments was independent from the person receiving the cheques and making those deposits at the bank. Automation, however, has advanced these activities (Moeller, 1997:257). Settlements of payments today are done through the internet or through electronic data interchange transactions. Organisations have been forced to rethink and where necessary, redesign some of their internal control standards or guidelines due to change in technology. The former approach has served organisations for many years, but due to the growth of highly integrated information systems it has somewhat become irrelevant. These changes called for the need to have a formal definition of internal controls.

## 2.2 What are the Internal Controls?

Internal control is defined as a "process designed, established and monitored by those charged with governance, management and other personnel" (Jackson & Stent, 2016:5/5). The main objective of internal control is to assist organisations to achieve reasonable assurance about achievement of organisations' objectives. This definition was further expanded by Coetzee, Bruyn, Fourie & Plant (2012:109), who defined the internal control as "procedures and plans that have been reviewed and accepted by management in order to assist in achieving management's goal to ensure that the business of an organisation are properly conducted in a proper and orderly manner."

A more widely adopted and comprehensive definition is given by the Committee of Sponsoring Organisations (COSO) of the Treadway Commission.

The Treadway Commission is composed of the Institute of Internal Auditors (IIA), the American Institute of Certified Public Accountants (AICPA), Financial Executives International (FEI), the American Accounting Association (AAA), and the Institute of Management Accountants (IMA). From the Treadway Commission, COSO was formed as a joint initiative with the Treadway Commission, and this organisation has focused on providing internal control guidance to firms (Wilford, 2012:7).

COSO defines internal control as "a process, effected by an entity's management, board of directors, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives" (COSO, 2017). The categories for these objectives are efficient operations, reliable financial reporting, and compliance with laws and regulations. Control is further defined as any action that is taken by the board, management and other parties in order to manage risk and increase the possibility of achieving organisation goals (Coetzee, Bruyn, Fourie & Plant, 2012:109).

In recent years, organisations have been more attentive and interested in the role that internal controls play (Agbejule & Jokipii, 2009:500). Internal controls are not solely about policy and procedure manuals and systems, they are also about individual behaviour and actions that they portray that affect internal control at every level of an organisation. The COSO's definition is very clear in that internal control is a process effected by every employee in an organisation, and therefore no one within an organisation is exempt. Thus, it is important that once controls are established, they are presented on paper and communicated to all staff members who are then required to adhere to the policies and procedures. Training has been found to be an imperative element in ensuring the effectiveness of internal controls (AICPA, 2014:8).

As stated by Dalkin (2013:5) factors outside management's influence or control can impact on the achievement of an organisation's goals. For example, a natural disaster is outside management's control, this can affect an organisation's ability to achieve its objectives. Therefore, once effective internal controls are in place, they provide reasonable assurance that an organisation will achieve its objectives. And lastly, "that internal control should be adaptable to an organisation's structure, and thus flexible in application" (COSO, 2013:3). Lakis

and Giriūnas (2012:149), and majority of other authors, assert that internal control is a holistic activity in both financial and management accounting. Sambo (2019:123) states that municipalities used the services of consultants and auditors, in their effort to obtain unqualified financial statements. According to Baloyi & Beyers (2019:468) in order to direct functions, daily sufficient internal control measures should be in place. Furthermore, findings by Dzomira (2017) indicate that inadequate financial governance in the Republic of South Africa continues to contribute to the incurrance of unauthorised expenditure.

### 2.3 Components of Internal Controls

Many entities (e.g. firms, government agencies), recognising the importance of controls, have adopted the categories of internal control developed by COSO (i.e. "control environment, control activities, risk assessment, information and communication, and monitoring") to structure their internal control evaluations (August-Crook, 2009:4). According to

August-Crook (2009:1), the planning and assessment of the effectiveness of internal control indicates that organisations may use a structure other than COSO. However, it also emphasises the significance of the COSO framework, as evidenced by the many organisations using the framework (Klynveld Peat Marwick Goerdeler (KPMG), 2004).

The COSO framework has 17 explicit principles that enhance management's understanding of what constitutes effective internal control (COSO, 2017:3). Table 1 below illustrates the 17 principles and related components of the COSO framework.

Each principle stated in Table 1 is suitable for all organisations and they are considered important and relevant, unless there is a set exception. "...If you don't have these key principles, then you don't have a successful internal control structure" (Aquila, 2013: 24). To check whether a principle is present and functioning, the intention of the principle and how it is being applied must be understood. It must then work to assist personnel understand and apply the

**Table 1: Components of Internal Control**

| Components                       | Principles  |
|----------------------------------|---|
| 1. Control environment           | "A set of standards, processes and structures that provide a basis for carrying out internal control in an organisation."<br>1. "Tone at the top: this represents the integrity and ethical values of the organisation<br>2. Exercises oversight responsibility<br>3. Establishes structure, authority, and responsibility<br>4. Process of attracting, developing and retaining competent individuals<br>5. Enforces accountability"             |
| 2. Risk assessment               | "A dynamic and iterative process for identifying and assessing risks to the achievement of objectives."<br>6. "Specifies suitable objectives related to operations, reporting and compliance<br>7. Identifies and analyses risk to those objectives<br>8. Assesses fraud risk<br>9. Identifies and analyses significant changes that may render internal control ineffective"   |
| 3. Control activities            | "The actions established through policies and procedures that help ensure that management's directives to mitigate risks are carried out and the achievement of objectives is reached."<br>10. "Selects and develops control activities within all business processes<br>11. Selects and develops general controls over technology<br>12. Example, authorisation/ approvals, reconciliation and segregation of duties"                            |
| 4. Information and communication | "Information is necessary for an organisation to carry out internal control responsibilities in support of achievement of its objectives."<br>13. "Organisation obtains and uses relevant, quality information to support the functioning of internal control<br>14. Internally communicates information, i.e. Objectives and internal control responsibilities<br>15. Externally communicates matters affecting functioning of internal control" |
| 5. Monitoring                    | "Ongoing evaluations to determine whether each of the five components of internal control are present and functioning."<br>16. "Conducts ongoing and/or separate evaluations<br>17. Evaluates and communicates deficiencies"  |

Source: Committee of sponsoring organisations (2017: 5)

principle consistently throughout the organisation, as any weaknesses require management's attention (COSO, 2017:5).

## 2.4 Types of Municipalities in South Africa

Thornhill (2012:133) cites that "South Africa's democratic election in 1994 ushered with it a new system of government that consists of three spheres of government – national, provincial and local – which are interdependent and interrelated." In this regard, section 151 of the Constitution of 1996 gives effect to the establishment of the local sphere of government, which consists of municipalities throughout the country. According to Sambo (2019:116) "the objectives of the local sphere of government are to ensure that services are provided to communities in a sustainable way, as well as the promotion of social and economic development (RSA, 1996:74). The Local Government: Municipal Structures Act, 117 of 1998 is the statute that provides for the establishment of the various categories of municipalities as described above."

Chapter seven of the Constitution of South Africa mandates that every province must have a municipality. The municipalities were categorised into three categories, namely: "Category A, referred to as metropolitan municipalities which have exclusive municipal executive and legislative authority in their areas, Category B, referred to as local municipalities, share municipal executive and legislative authority in their areas with Category C municipalities within whose areas they fall. Category C, referred to as district municipalities, have municipal executive and legislative authority in areas that include more than one municipality."

According to AGSA (2016:18), municipalities should have systems in place that encourage and enforce compliance to ethical values and have respect for the law especially because they are accountable to the public. The concept of the public interest and accountability are imbedded in the country's constitution and other legislation that governs local governments (AGSA, 2016). In order to adhere to the constitution, municipalities should comply with directives given by AGSA in implementing these mechanisms or controls to ensure an ethical environment and compliance with the rules and regulations. It is management' responsibility to enforce policies that will direct conformance to all policies implemented within municipalities.

## 2.5 Types of Controls

There are four types of controls such as directive, preventative, detective and corrective.

**Directive** – These are 'soft' controls, which are embedded within the culture of an organisation and are designed to ensure that a particular outcome is achieved. Although this type of control encourages positive behaviour it does not however prevent or detect undesirable events, for example, by emphasising the code of conduct, value statement, ethics, policies, performance guidelines, education and training (Wallis, 2012:42).

**Preventive** – "These controls prevent loss or harm from occurring. For example, a control that enforces segregation of duties" (an employee with the responsibility of submitting a payment request, should get another employee or supervisor to authorise it before submission), this will minimise the possibility of an employee issuing fraudulent payments (Wallis, 2012:42).

**Detective** – These controls monitor activities in order to identify situations where certain procedures have not been followed. For example, a business failing to reconcile the general ledger or inability to identify fraudulent payments due to not reviewing payment request audit logs, exception reports, monitoring and oversight controls (Wallis, 2012:42).

**Corrective** – Controls that restore the system back to the original state before a harmful event (Scholtz, 2014:64). An example would be a business implementing a full restoration of a system from backup tapes after evidence is found that the payment data, insurance payments and business recovery plan have been improperly altered.

According to AGSA (2016:183), in order to ensure reliable financial and performance reporting and compliance with legislation AGSA assesses internal controls to determine the effectiveness of their design and implementation. This forms part of their audit process. Bhana and Ngoepe (2009:20) assert that, when an auditor can arrive at an organisation or company they are auditing, they must be provided with the audit file without any hesitation containing financial statements necessary is a resemblance of an ideal audit environment. The financial statements should in turn be cross-referenced, to all their relevant supporting documents

in the same file, or an indication of where such records can be easily retrieved must be clearly referenced.

### 3. Methods and Materials

A qualitative research study was conducted through analysing the AGSA's reports for 2015/2016 financial year using a content analysis method to determine the internal controls underpinning the audit outcomes in South African municipalities. The AGSA reports were important in solving the paper's problem statement. The AGSA's reports for the period 2015/2016 financial year were collected with the assistance of Atlas.ti software. These data were collected from all the three categories of municipalities in South Africa, namely, metropolitan, district and local municipalities. The main theme formulated in gathering the data was on internal controls underpinning the positive audit outcomes in municipalities in South Africa. This was done in order to determine what the main AGSA's findings are with regards to the main internal controls underpinning the achievement of positive audit outcomes in South African municipalities.

The ethical clearance was obtained through the University of Johannesburg's Ethics Committee, although this was not necessary as the data collected and used is publicly available for public use. A qualitative research design using document analysis was implemented to achieve the research objectives. Data was collected through secondary data available in the public domain. The criterion sampling method was used for metropolitan municipalities whilst simple random sampling method was used for district and local municipalities. The data was analysed by means of coding the collected AGSA's data to allow the identification of themes and subthemes. "Coding in qualitative research consists of the assignment of short phrases to capture a meaning of a large portion of textual data" (Yin, 2011). Saldaña (2009:8) and Babbie (2013:550) define coding "as a process of arranging raw data into a standardised form." The process started with a review of AGSA reports for 2015/2016 financial year. While considering the whole context, the data was coded.

### 4. Results and Discussion

After concluding the analysis of the AGSA audit reports for 2015/2016 financial year, the following main findings were raised with regard to internal controls underpinning the audit outcomes in

South African municipalities. The paper refers to Unqualified (clean) and Qualified, Adverse and Disclaimer of opinion (as unclean) audits.

- **Unqualified audit opinion:** Financial Statements fairly present the financial position and results (Auditor is happy with financial statements as a whole).
- **Qualified audit opinion:** Financial statement fairly present financial position, except for i.e. Inventory (Auditor is happy with financial statements as a whole except for one or two sections).
- **Adverse audit opinion:** Financial Statements do not fairly present the financial position (Auditor is overall unhappy with financial statements).
- **Disclaimer of opinion:** Auditor is not in a position to even give an opinion for various reasons (i.e. scope limitation).

#### 4.1 Human Resource (HR) Management and Use of Consultants

The objective of the analysis in Table 2 is to contrast HR management controls and the use of consultants between clean and unclean audits.

In Table 2 on the next page, it is evident that municipality 1 is the only municipality that invested in consultants in their finance department. The municipality ensured effective use of consultants through knowledge transfer to their own staff within the finance department. All municipalities with a clean audit outcome continue to invest in staff development by providing training opportunities to staff members. Key positions such as those of COO, CEO and CFO are filled within three months. Finance management programmes have been funded for the three-year minimum municipal competency programme for lower staff levels, to enhance the development of competent employees within the finance environment. These municipalities seem to have implemented HR policies, and those in key positions ensure compliance thereof.

In Table 3 on the next page, although municipality 6, 10 and 12 at 75% almost met all criteria specified under Human Resources control as given by the researcher, their investment in consultants was due to over-reliance on consultants to compile financial statements. This resulted in leadership failing to

**Table 2: HR Management Controls and Use of Consultants for Municipalities with Clean Audits**

|                        | Key financial positions filled | Investment in staff development | Compliance with HR policies | Investment in consultants | Total yes | %   |
|------------------------|--------------------------------|---------------------------------|-----------------------------|---------------------------|-----------|-----|
| <b>Municipality 1</b>  | Yes                            | Yes                             | Yes                         | Yes                       | 4         | 100 |
| <b>Municipality 2</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 3</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 4</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 5</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 6</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 7</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 8</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 9</b>  | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 10</b> | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |
| <b>Municipality 11</b> | Yes                            | Yes                             | Yes                         | No                        | 3         | 75  |

Source: Researchers' own compilation, Atlas.ti V8 (2020)

**Table 3: HR Management Controls and Use of Consultants for Municipalities with Unclean Audits**

|                        | Key financial positions filled | Investment in staff development | Compliance with HR policies | Investment in consultants | Total Yes | % Yes |
|------------------------|--------------------------------|---------------------------------|-----------------------------|---------------------------|-----------|-------|
| <b>Municipality 1</b>  | No                             | N/A                             | N/A                         | No                        | 0         | 0     |
| <b>Municipality 2</b>  | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 3</b>  | No                             | N/A                             | N/A                         | No                        | 0         | 0     |
| <b>Municipality 4</b>  | No                             | Yes                             | N/A                         | No                        | 1         | 25    |
| <b>Municipality 5</b>  | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 6</b>  | No                             | Yes                             | Yes                         | Yes                       | 3         | 75    |
| <b>Municipality 7</b>  | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 8</b>  | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 9</b>  | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 10</b> | No                             | Yes                             | Yes                         | Yes                       | 3         | 75    |
| <b>Municipality 11</b> | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 12</b> | No                             | Yes                             | Yes                         | Yes                       | 3         | 75    |
| <b>Municipality 13</b> | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 14</b> | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 15</b> | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 16</b> | No                             | Yes                             | Yes                         | No                        | 2         | 50    |
| <b>Municipality 17</b> | No                             | Yes                             | Yes                         | No                        | 2         | 50    |

Source: Researcher's own Compilation (2020)

monitor skills transfer to municipal financial officials. Consequently, financial statements still had material misstatements where consultants performed the work, which resulted in increased audit time and cost.

Secondly, although HR policies were developed, due to lack of leadership some of these policies were not implemented. A few municipalities had their policies drafted, however, they were awaiting

approval. This may have resulted in thorough screening of employees in the finance department being overlooked or not prioritised, therefore the preventative control of employing unskilled staff may have been ineffective, hence the use and reliance on consultants. Thirdly, where investment in staff development was concerned, two municipalities in this category reported that staff were reluctant to follow through with training and other

developmental projects. Other municipalities faced challenges with staff members who were reluctant to complete annual skills audits, despite significant amounts of money being spent on skills development plans.

All municipalities in this category reported that they had been unsuccessful in filling permanent vacancies with suitably qualified candidates. Findings revealed that the high demand for consultants serves as evidence of a competency gap, and this has resulted in municipalities not prioritising filling of those vacant positions. In addition, over-reliance on consultants is an indication of a lack of expertise and capacity in municipalities to produce unqualified financial statements. In a study by Ngoepe (2012), findings revealed that consultants compiled financial statements due to lack of financial skills at municipalities, of which those consultants did not always provide skills transfer and because of this, the same consultants were contracted the subsequent years.

Most municipalities had adequate internal controls to manage their environments, as can be seen in Table 4 below.

According to Motubatse (2019:120) internal audit needs IT capabilities, therefore, because IT can affect the ability of an organisation to operate successfully, there is a need for internal auditors to enhance their IT skills. Such skills will assist in the audit process. All municipalities had efficient

IT infrastructure with a CIO or qualified IT specialist overseeing the IT department. It is worth noting that their supporting documents were readily available, which evidenced a link between stability in key positions, good IT infrastructure and record-keeping. Municipalities 4, 6 and 10 are at 83% due to moderate monitoring compliance control. The internal audit function (one of the assurance providers) of municipality 3, had the municipality's compliance with IIA standards assessment outstanding. In addition, the quality assurance review of the internal audit unit was not completed.

As Shown in Table 5 on the next page, municipalities that obtained an unclean audit indicated that those in key positions in the IT department, i.e. the CIO or IT manager, did not qualify or have adequate years' experience for the position. This in turn contributed to areas of concern with regard to IT controls. In order for these municipalities to fulfil their IT roles and responsibilities they had to make use of consultants whose performance was not monitored.

Other municipalities did not establish an IT governance framework or isolate security vulnerabilities. Since their IT steering committees were inactive, action plans were not being employed and monitored, and lack of testing for the disaster recovery plans failed to ensure data recovery in the event of a disaster. Inadequate management oversight caused non-implementation of prior commitments. There were no policies and procedures designed or implemented, as it was the case in previous years.

**Table 4: IT Systems Review and Monitoring Compliance and Record-Keeping of Municipalities with Clean Audits**

|                        | IT System | Review and monitoring compliance | Record keeping | Total Yes | % Yes |
|------------------------|-----------|----------------------------------|----------------|-----------|-------|
| <b>Municipality 1</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 2</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 3</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 4</b>  | Good      | Moderate                         | Good           | 2.5       | 83    |
| <b>Municipality 5</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 6</b>  | Good      | Moderate                         | Good           | 2.5       | 83    |
| <b>Municipality 7</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 8</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 9</b>  | Good      | Good                             | Good           | 3         | 100   |
| <b>Municipality 10</b> | Good      | Moderate                         | Good           | 2.5       | 83    |
| <b>Municipality 11</b> | Good      | Good                             | Good           | 3         | 100   |

Source: Researchers' own compilation (2020)

**Table 5: IT Systems Review and Monitoring Compliance and Record-Keeping for Municipalities with Unclean Audits**

|                        | IT System  | Review and monitoring compliance | Record keeping | Total Yes | % Yes |
|------------------------|------------|----------------------------------|----------------|-----------|-------|
| <b>Municipality 1</b>  | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 2</b>  | Good       | Good                             | Inadequate     | 2.25      | 75    |
| <b>Municipality 3</b>  | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 4</b>  | Inadequate | Good                             | Inadequate     | 1.5       | 50    |
| <b>Municipality 5</b>  | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 6</b>  | Good       | Moderate                         | Inadequate     | 1.75      | 58    |
| <b>Municipality 7</b>  | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 8</b>  | Moderate   | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 9</b>  | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 10</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 11</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 12</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 13</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 14</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 15</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 16</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |
| <b>Municipality 17</b> | Inadequate | Moderate                         | Inadequate     | 1         | 33    |

Source: Researchers' own Compilation (2020)

At some municipalities the security controls were compromised therefore they experienced security breaches, which resulted in fraudulent activities. General access control was not always reviewed, and thus unfortunately separation of responsibilities was not consistently maintained. The researcher deduced that IT controls are an inherent part of the control environment in municipalities. They enable efficiency in service delivery, promote security and trustworthiness in financial statements, ensure confidential, fair and available state information. Unfortunately, management had not implemented proper record-keeping and IT controls to ensure that complete, accurate, and relevant information was accessible and available to support financial reporting.

## 5. Conclusion and Recommendations

Based on the information presented above, it is evident that the municipalities' leadership, with the assistance of municipal officials, have not prioritised addressing internal control weaknesses. Lack of leadership and accountability appears common in municipalities with unclean audits. Instead of

appointing qualified officials, management allocates a substantial amount of money and resources to consultants, who are not monitored and consequently do not transfer skills to the municipalities' accounting officers which indicates serious lack of directive and preventative controls. The control environment as one of the important preventative internal control component is compromised at certain municipalities due to a high vacancy rate in key management positions. This has resulted in insufficiently implemented and monitored internal controls, leading to security breaches and fraudulent activities.

It is, therefore, recommended that all municipalities in South Africa need to design and implement both directive and preventative internal controls for the achievement of the stated objectives. Furthermore, effective leadership fosters a culture of ethical behaviour and commitment to good governance. The researcher recommends that the municipal management should consider applying the King IV report on governance in order to enhance ethical culture, effective control, legitimacy, and good performance.

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