

Public Sector: Accounting and Finance

Presenters: Caryn Maitland CA(SA)
Bronwyn MacCallum CA(SA)

Session 3: Risk management and internal controls

Understanding the requirements for and process of risk management in the public sector, and how internal controls are used to manage risk

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Caryn Maitland

Caryn is a qualified CA(SA and RA, who has lectured extensively at UKZN (and other institutes) where she lectured Advanced Financial Accounting up until 2011 as well as co-ordinating the module on the Pietermaritzburg campus and was appointed Section Head of Financial Accounting and Deputy Head of the School of Accounting (managing the Pietermaritzburg campus) prior to leaving UKZN.

She has conducted independent workshops and seminars for professional accountants since 2006 on various topics and has consulted on a number of technical issues. Since January 2011, she has focused on her own business as technical freelance consultant and trainer to those working within the accounting profession. Caryn is a technical advisor to the SAICA Eastern Region Midlands District, Northern District and Southern District Associations, as well as the Small Practice Interest Group in Durban – specialising in financial reporting (IFRS, IFRS for SME's and general accounting), assurance, legislation and ethics. Caryn has a passion for Corporate Governance, which together with her Companies Act specialism and Financial Management for Non Financial Management lecturing background, has served her well in consulting and advising various Boards of Directors in recent years.

Caryn is also a platform presenter for various institutes as well as many small to medium accounting practices across the country and into Southern Africa. Maitland was appointed as a visiting Associate Professor to the University of Limpopo tasked with mentoring their Financial Accounting staff (Aug 2011 to Dec 2013).

Maitland's passion is IFRS and IFRS for SME's and was delighted at the opportunity granted in 2013 to serve on the APC subcommittee constituted to investigate the need for Micro GAAP and the role of IFRS for SME's for small and medium sized practitioners. Caryn, also serves on the Joint Accountants, Auditors and Attorneys Committee of SAICA, and is part of the School Governing Body project initiated by SAICA in KwaZulu-Natal, and has been appointed as an alternative member to the APC in June 2020

Caryn was elected as the first woman Chairperson for the Midlands District Association for SAICA in 2018 and also serves on the Eastern Region SMP Committee as well as the Local Subvention Committee for SAICA. In 2019 Caryn was appointed to the SAICA Eastern Region Council. As someone who is committed to environmental affairs, Caryn serves as a non-executive director for the Institute of Natural Resources, a Non Profit Company focusing on research. Since 2018 Caryn has worked extensively with commerce and industry, assisting analysts, directors and other users of financials to interpret, prepare, analyse and forecast based on the results of financial statements.



Bronwyn MacCallum

Bronwyn qualified as a CA(SA) in 2004 and has spent time in private practice as a partner and later director of small and medium firms as well as a tenure at the Auditor-General of South Africa as a Senior Manager and SAICA Training Officer. Her current professional focus is on the design, implementation and monitoring of systems of quality control in the auditing profession for firms and for engagements.

Bronwyn has also spent many years lecturing Auditing, IFRS and Public Financial Management at undergraduate, post-graduate and professional levels, both face to face and in the design and implementation of blended and on-line learning platforms. Bronwyn has played active roles at both SAICA and IRBA in board sub-committees related to professional practical training and development, and in various public sector governance structures and audit committees.

Bronwyn has significant experience in auditing in the public sector in South Africa, in audit committee and financial misconduct governance structures and speaking and presenting to political oversight structures. Bronwyn has also had extensive experience in the authoring and quality assurance processes of professional learning content for public finance management and related disciplines in government for the English speaking African countries. Topics include accounting and auditing in the public sector, public sector context, public financial management, financial management, economics, performance management, ICT and communications.

The content and training materials prepared and delivered have catered to both qualified accounting professionals working in the public sector, as well as to long-serving public servants who have not been formally trained in PFM, accounting and finance in the public sector.



Course Outline

Session Objectives

- Understand the theory of risk management in the public sector
- Understand the process for risk management
- Understand how risks are responded to
- Understand the role players in the risk management process
- Understand how internal controls are used to manage risk

Programme

- What is risk?
- What is business risk?
- What is risk in the public sector?
- What is risk management?
- How do we manage risk?
- The risk management process
- Types of risk
- How do we respond to risk?
- Role players in the risk management process
- Internal control as a risk response

What is risk?

A **probability or threat** of **damage, injury, liability, loss**, or any **other negative occurrence** that is **caused** by external or internal vulnerabilities, and that **may be avoided** through **pre-emptive action**.

What is business risk?

In business, risk means that a company's or an organization's plans may not turn out as originally planned or that it may not meet its target or achieve its goals, for example:

- Growth
- Revenue targets
- Market share
- Share price

What is risk in the public sector?

- International organisation for Standardization (ISO) which in its standard 31000:2018 defines risk as “**the effect of uncertainty on objectives**”
- Public sector objectives:
 - Service delivery in terms of the rights enshrined in our Constitution
 - defeat the COVID-19 pandemic;
 - accelerate economic recovery;
 - implement economic reforms to create sustainable jobs and drive inclusive growth; and
 - fight corruption and strengthen the State

What is risk in the public sector?

- Risk:
 - Measures the probability and severity of damages/losses etc
- Uncertainty:
 - lack of definite knowledge, a lack of sureness; doubt
- Effect:
 - uncertainty itself can be measured in terms of probability or likelihood, *whereas the effect would be the consequence or the impact of the uncertainty*

Example of public sector risk

- Objective:
 - To deliver sufficient supply of quality potable water to the resident of a municipality
- Uncertainty:
 - Sufficiency of supply (or water availability)
 - Proliferation of water-borne bacteria
- Effect of the uncertainty:
 - Residents to not have access to water (water scarcity)
 - The water is contaminated and results in a cholera outbreak

Types of risk in the public sector

- Strategic risk
- Operational risk
- Financial risk
- Compliance risk

Strategic risk

Strategic risk

- Relate to the achievement of an organisation's objectives
- Consequence: organisational failure and even closure
- Business risks – relate to the products or services that the organisation provides
- Non-business risks – relate to other matters, for example, risks associated with the long-term sources of finance used

Operational risk

Operational risk

- the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events
- operational risk is the risk contained in the everyday activities of an organisation
 - business interruption
 - errors or omissions by employees
 - product failure
 - health and safety
 - failure of IT systems
 - fraud
 - loss of key people
 - litigation
 - loss of suppliers

Financial risk

Financial risk

- (Treasury): ***Financial risk management***: to manage limited financial resources with the purpose to ensure economy and efficiency in the delivery of outputs required to achieve desired outcomes (effectiveness), that will serve the needs of the community (appropriateness)
- Financial risk: arises from failure to managing finance in accordance with requirements and financial constraints
- Consequences:
 - poor returns from investments
 - failure to manage assets/liabilities (for example debt collection, losses/theft)
 - failure to obtain value for money
 - non-compliant financial reporting

Compliance risk

Compliance risk

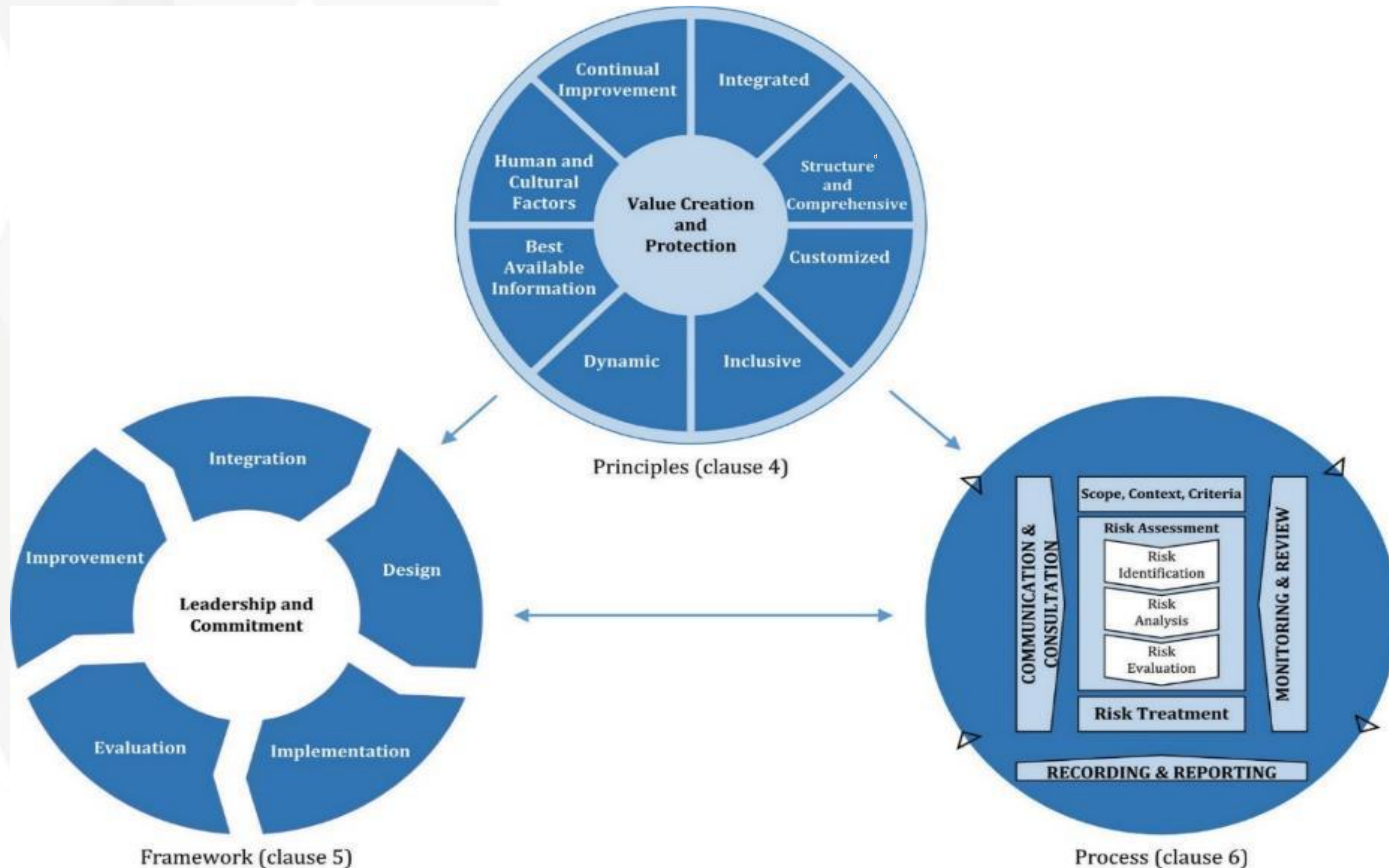
- the risk of non-compliance with laws and regulations
- Compliance-driven environment: Public sector financial management, operational (health and safety, labour), industry (eg water, health, safety etc)

How do we manage risk?

Principles of the risk management process (ISA31000):

- an iterative process
- assists organizations in setting strategy, achieving objectives and making informed decisions
- forms part of governance and leadership
- fundamental to how the organization is managed at all levels
- includes interaction with stakeholders
- considers the external and internal context of the organization, including:
 - human behaviour and cultural factors.
- based on the principles, frameworks and processes, adapted or improved so that managing risk is efficient, effective and consistent.

ISO31000 Risk Management Process



How do we manage risk?

- a) Integrated - Risk management is an integral part of all organisational activities.
- b) Structured and comprehensive - A structured and comprehensive approach to risk management contributes to consistent and comparable results.
- c) customised - The risk management framework and process are customised and proportionate to the organisation's external and internal context related to its objectives.
- d) Inclusive - Appropriate and timely involvement of stakeholders enables their knowledge, views and perceptions to be considered. This results in improved awareness and informed risk management.
- e) Dynamic - Risks can emerge, change or disappear as an organisation's external and internal context changes. Risk management anticipates, detects, acknowledges and responds to those changes and events in an appropriate and timely manner.
- f) Best available information - The inputs to risk management are based on historical and current information, as well as on future expectations. Risk management explicitly takes into account any limitations and uncertainties associated with such information and expectations. Information should be timely, clear and available to relevant stakeholders.
- g) Human and cultural factors - Human behaviour and culture significantly influence all aspects of risk management at each level and stage.
- h) Continual improvement- Risk management is continually improved through learning and experience. (ISO 31000)

The risk management process

Step1: Establishing the context

Step 2: Risk identification

Step 3: Risk assessment

Step 4: Risk evaluation

Step 5: Risk response

Step 6: Risk monitoring and reporting

Step 1: Establish context

- obtaining clarity regarding:
 - the *objectives* to be achieved, whether strategic, operational, financial or compliance
 - The context of the objectives and activities of within the organisation
 - organisational factors can be a source of risk
 - the context in which the organisation finds itself, in other words what is happening in the external environment (industry, economy, region, world)
- Use of tools:
 - SWOT analysis
 - PESTLE analysis (political, economic. socio-cultural, technological, legal and environment)
- Define and set risk appetite relative to objectives
- Define criteria to evaluate risk significance (based on a framework / policy)

Step 2: Risk identification

- to find, recognise and describe risks that might help or prevent an organisation achieving its objectives
- Techniques:
 - Brainstorming (most used for general risk identification this includes risk identification workshops)
 - Consequence/likelihood matrix
 - Human Reliability Analysis (HRA)
 - Primary or Preliminary Hazard Analysis (PHA)
 - Scenario Analysis (SA)
 - Structured What-If Techniques (SWIFT)
- Record risks in a risk register

ID	Date raised	Risk description	Likelihood	Impact	Severity	Owner	Mitigating action	Contingent action	Progress on actions	Status
1	12/12/15	There is a risk that assets may not be completed in time to meet production schedules.	Low	High	Amber	S. Scott	Agree writing days in advance, reallocate writer's other work. Agree to stagger delivery of chapters so that editing can start earlier.	Increase duration of Printing schedules & move from 4 col to 2 col.	Update 13/12/2015 mitigation actions implemented	Open

Step 3: Risk assessment

- Analysis: nature of risk and its characteristics – a detailed consideration of:
 - Uncertainties
 - risk sources
 - Consequences
 - Likelihood
 - events, scenarios
 - controls and their effectiveness
- Likelihood and consequences measured on a scale

Step 3: Risk assessment

- Likelihood/probability

Probability Rating	Criteria
Certain 5	99% probability, or <ul style="list-style-type: none">• impact is occurring now, or• could occur within “days to weeks”
Almost certain 4	>50% probability, or <ul style="list-style-type: none">• balance of probability will occur, or• could occur within “weeks to months”
Likely 3	>20% probability, or <ul style="list-style-type: none">• may occur shortly but a distinct probability it won’t, or• could occur within “months to years”
Possible 2	>5% probability, or <ul style="list-style-type: none">• may occur but not anticipated, or• could occur in “years to decades”
Unlikely 1	<5% probability occurrence requires exceptional circumstances exceptionally unlikely, even in the long term future only occur as a “100 year event”

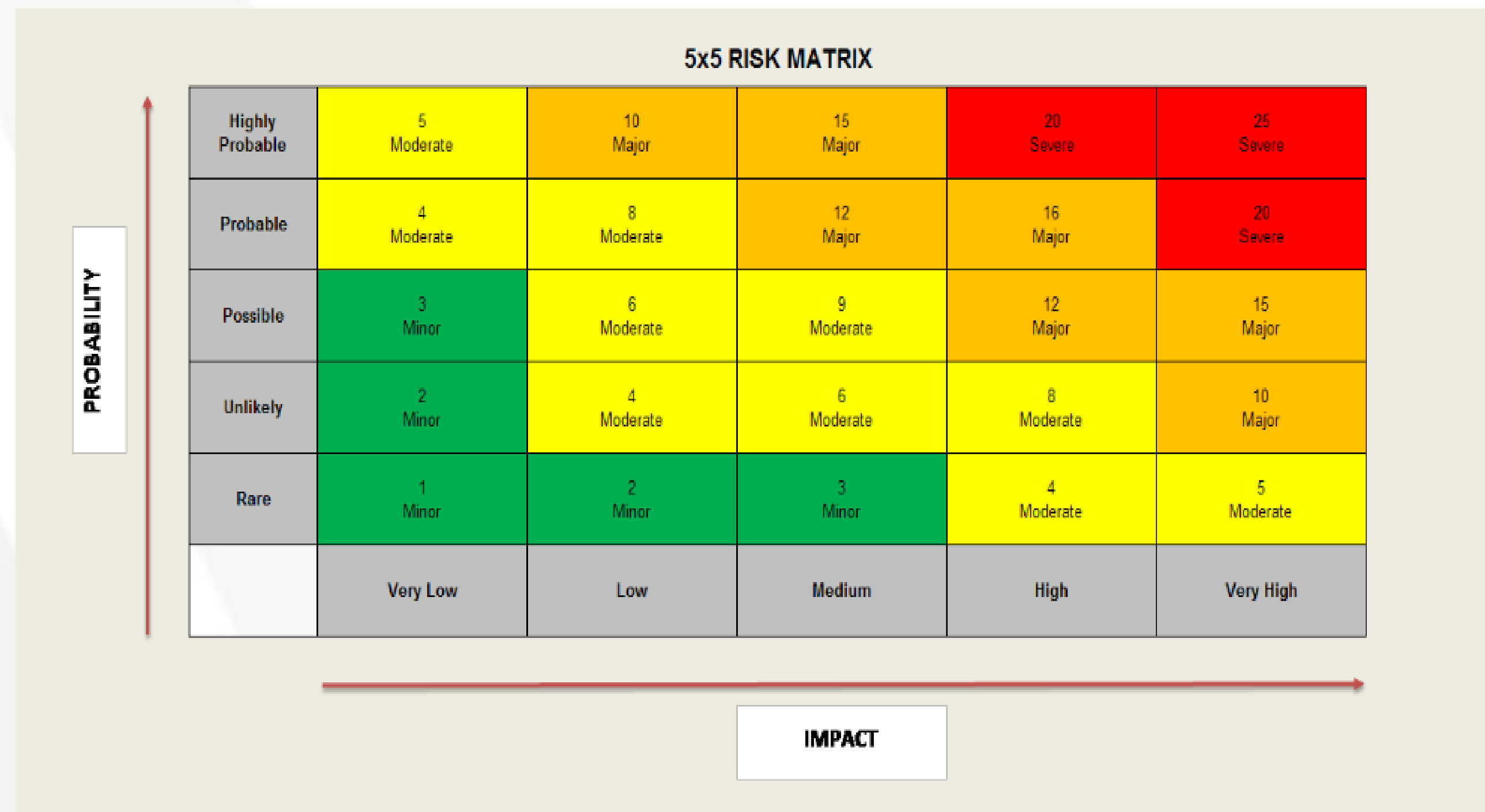
Step 3: Risk assessment

- Consequence

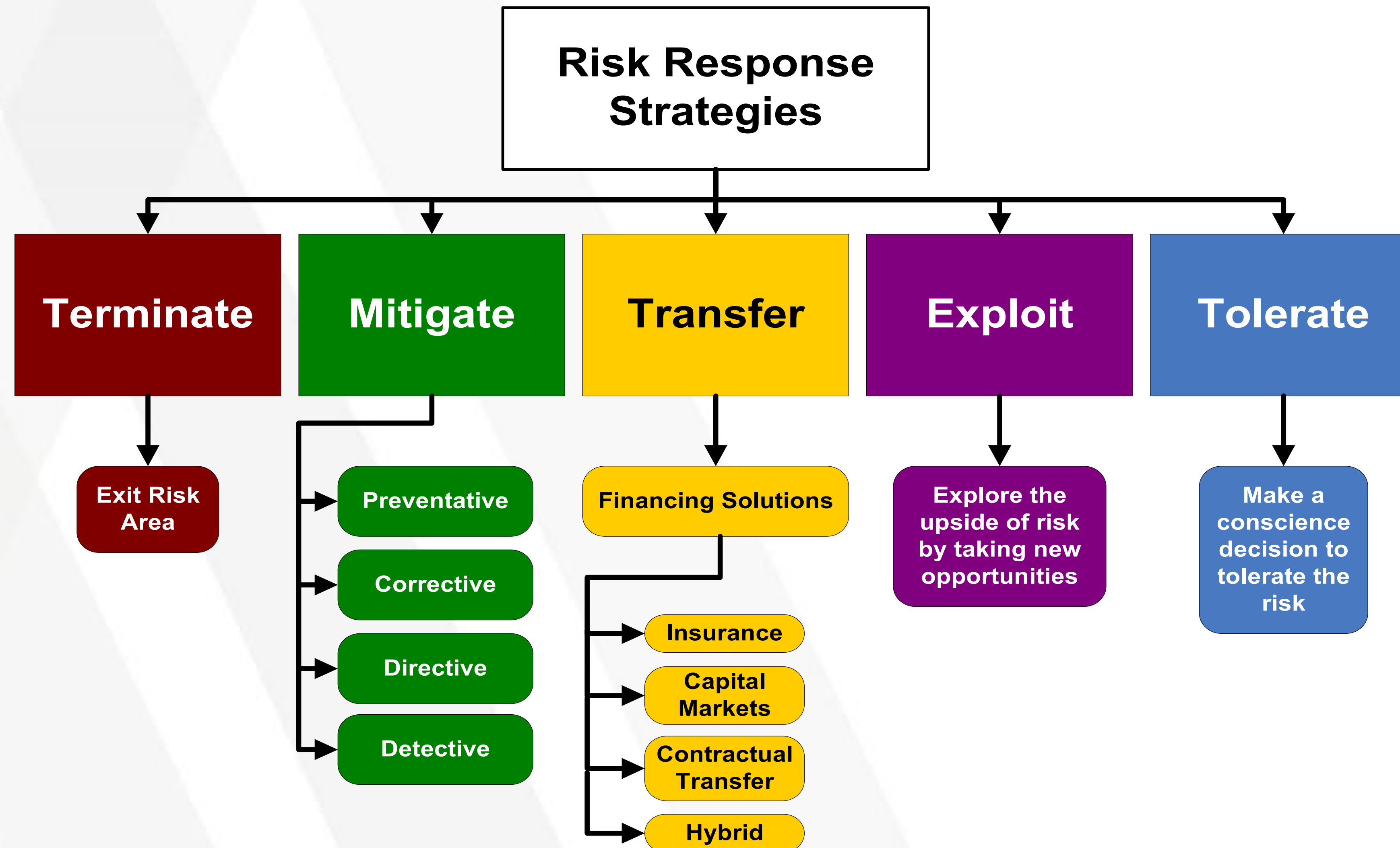
Consequence	Critical Success Factors					
	Safety	Quality of Services	Reputation	Environment	Cost	Legal/Contractual
Severe	Would cause loss of life.	Severe impact on the quality of services provided by the Council resulting in a significant increase in complaints from the community (increase of 50% or more).	External Reputation irrevocably destroyed or damaged. Severe impact on staff turnover (increase of >20% above average levels)	Would cause catastrophic environmental damage leading to fines against the Council and significant resources to rectify.	>2.5M	Legal. Numerous Major Litigations. Contract. Termination of Contract for default.
Major	Would cause serious casualties resulting in the long-term physical impairment of personnel.	Considerable impact on the quality of services provided by the Council resulting in a marked increase in complaints from the community (increase of 25-50%).	External Reputation severely damaged: considerable effort and expense required to recover. Major impact on staff turnover (increase of 10-20% above average levels)	Would cause extensive environmental damage requiring significant resources to rectify.	\$1M-2.5M	Legal. Single Major litigation or numerous Moderate Litigations. Contract. Receive written notice from the contractor threatening termination if not rectified.
Moderate	Would cause several casualties that require hospitalisation with no long-term effects.	Some impact on the quality of services provided by the Council resulting in an increase in complaints from the community (10-25%).	External Reputation damaged: some effort and expense required to recover. Moderate impact on staff turnover (increase of 10-20% above average levels)	Would cause some environmental damage requiring the allocation of some resources to rectify.	\$500k-1M	Legal. Single Moderate litigation or Numerous Minor Litigations. Contract. Receive verbal advice that, if breaches continue, a default notice may be issued.
Minor	Would cause several minor casualties that require medical attention off-site with no long-term effects.	Minor impact on the quality of services provided by the Council resulting in an increase in complaints from the community (<10%).	External Reputation minimally affected. Little effort or expense required to recover. Minor impact on staff turnover (increase of 5-10% above average levels)	Minor environmental damage. Rectification occurs from within existing budget.	\$100k-500k	Legal. Single Minor litigation. Contract. Results in meeting between two parties in which contractor expresses concern.
Insignificant	Would cause minor injuries that are able to be treated at the site with no long-term effects.	No impact on the quality of services delivered by Council.	External Reputation not affected. No effort or expense required to recover. No impact on staff turnover	No environmental damage.	\$0-100k	Legal. Threat of litigation requiring small compensation. Contract. No affect on contract performance.

Step 4: Risk evaluation

- Comparison of risk analysis and risk criteria (eg heat map / risk matrix)
- to support decision-making re additional actions/responses required to risk, for example:
 - do nothing further
 - consider risk response options;
 - undertake further analysis to better understand the risk;
 - maintain existing controls; and
 - reconsider objectives.



Step 5: Risk response



Step 5: Risk response

Risk response plan:

- Risk Source
- Response strategy/ies selected
- Activities
- Target completion date
- Responsible person
- Actual date of completion
- Performance measures (Key risk indicators)

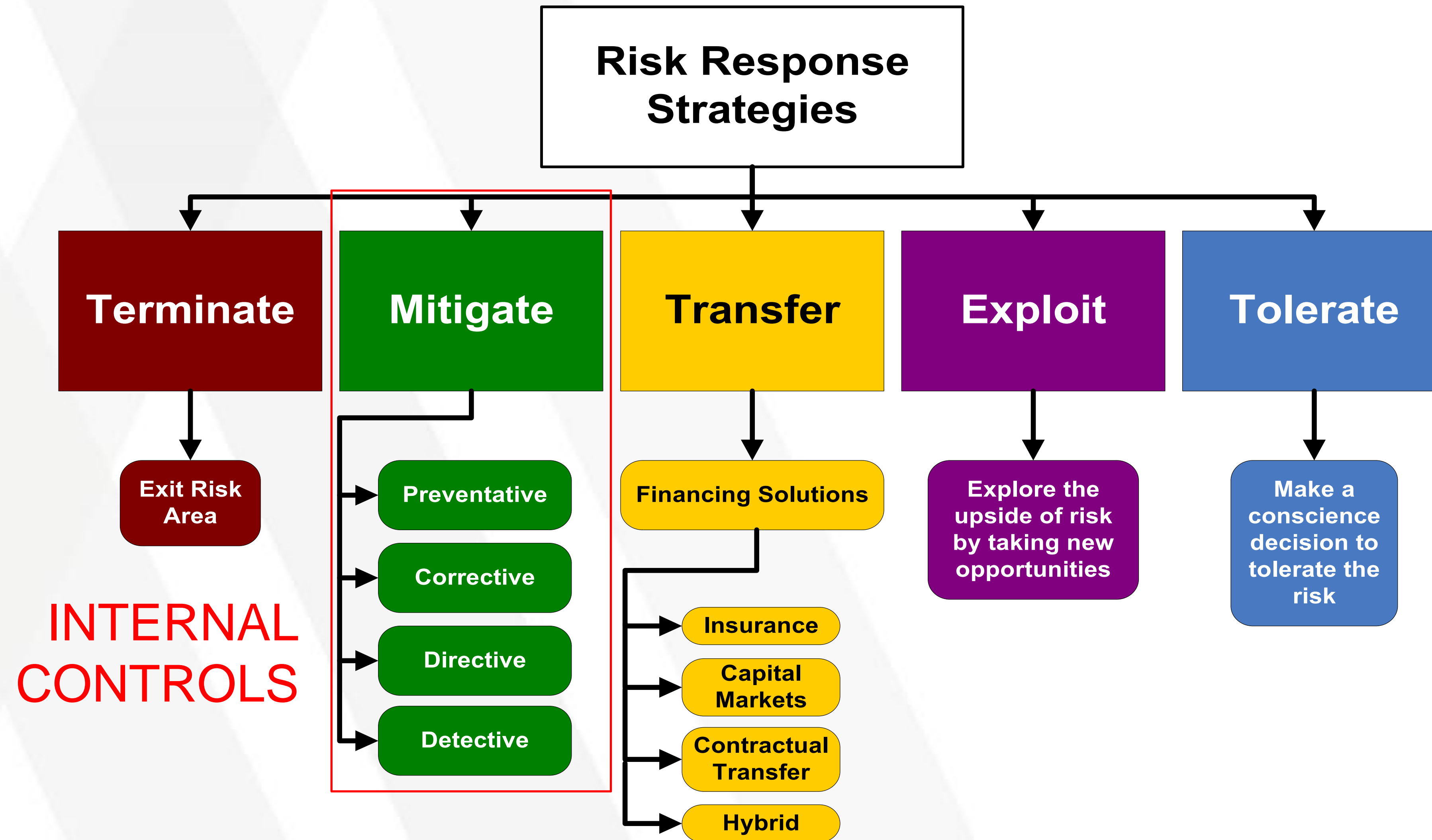
Step 6: Monitoring and reporting

- Planning, gathering and analysing information, recording results and providing feedback
- incorporated throughout the organisation's performance management, measurement and reporting activities
- Assists management to improve their risk management system
- Inputs include:
 - Audit findings (internal and external) (systems of internal control)
 - Non-compliance issues against the existing rule, regulation and standard
 - Risk observation, including the result of the assessment on the performance of risk management system
 - Progress of improvements recommended by a previous audit (follow up report)

Role players in risk management

- All people on a day-to-day basis
- Accountability and responsibility for the process:
 - Executive leadership of an entity
 - Head of department
 - Chief executive officer
 - Accounting officer
 - The audit or audit and risk committee
 - Internal audit
- National Treasury

Internal control as a risk response



Internal control as a risk response

- Mitigation: this is the most used strategy to address risk and it normally involves the institution of controls to counter risk and reduce its possibility
- Safeguarding of assets (loss, misuse, misappropriation, fraud, productivity)
- Reliability and integrity of information (financial, performance, compliance)
- Ensure compliance (PFMA, TR, other – processes, SOPs, timing, reporting)
- Efficiency and effectiveness of operations (responsibility, budget, quality, monitoring, reporting)
- Monitoring (internal audit, audit committee)
- Reporting (timing, financial, performance, compliance)

Internal control as a risk response

- PFMA s381(a)(i): (Accounting officer's responsibilities): *effective, efficient and transparent systems of financial and risk management and internal control;*
- PFMA s45(a): (Any other official): *must ensure that the system of financial management and internal control established for that department, trading entity or constitutional institution is carried out within the area of responsibility of that official;*
- *Treasury regulations:*
 - *Audit committees and internal audit*
 - *Planning and budgeting*
 - *Revenue and expenditure management*
 - *UIFW*
 - *Asset and liability management*
 - *Accounting and reporting*

Internal control as a risk response

- *Example: Expenditure management:*
 - *Requisition - Confirmation of project and budget (strategic, operational)*
 - *Order after three quotations (compliance, operational)*
 - *Receipt of goods (operational, financial, compliance)*
 - *Project management (strategic, operational)*
 - *Payment requisition (operational, financial)*
 - *Payment approval (financial, compliance)*
 - *Expenditure recording (financial)*
 - *Expenditure reporting (financial, operational)*
 - *Performance reporting (operational, strategic)*

Recap

- . Risk management in the public sector
 - . Uncertainty and impact
- . Risk types
 - . Strategic, operational, financial, compliance
- . Risk management
- . Risk management process
- . Risk management role players
- . Internal control as a risk response

Q&A

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