Topic: Asset Management Controls That Prevent Material Irregularities

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PRESENTATION LAYOUT

- OBJECTIVE
- LEGISLATIVE AND ACCOUNTING FRAMEWORK
- INTRODUCTION: ASSETS
- INTERNAL CONTROLS
- KEY CONTROLS: ASSETS MANAGEMENT CYCLE
- MATERIAL IRREGULARITIES (MIs)
- AUDIT OUTCOMES AND ACCOUNTABILITY

OBJECTIVE

The objective of this presentation:-

- Enhance awareness and understanding of asset management controls that are necessary to safeguard municipal assets, ensure compliance with applicable legislation and accounting standards, and support credible financial reporting,
- Highlight key risks associated with weak asset management practices,
- Demonstrate how deficiencies in asset management can lead to Material Irregularities, financial losses, and service delivery failures,
- Outline the roles and responsibilities of management, officials, and oversight structures in establishing and maintaining effective controls,
- Promote accountability, strengthen governance, improve audit outcomes, and ensure that municipal assets are managed efficiently and effectively throughout their lifecycle to protect public resources and support sustainable service delivery.

LEGISLATIVE AND ACCOUNTING FRAMEWORK

- Municipal Finance Management Act (MFMA),
- Municipal Systems Act
- GRAP Standards
- mSCOA Framework
- Public Audit Act 25 of 2004 as amended,

INTRODUCTION: ASSETS

- What are Infrastructure assets?
- What are internal controls?
- What are the benefits of internal controls?
- What are the key Internal controls within the Asset Management cycle?

INTRODUCTION: ASSETS

- **What is an asset?**

An asset is any resource owned or controlled by a municipality that can be used to provide services, generate revenue, or support municipal operations in the future.

Examples of Municipal Assets

- Infrastructure Assets,
- Community Assets
- Operational Assets
- Municipal Assets

- **What is an Infrastructure Asset?**

An infrastructure asset is a type of municipal assets/ PPE that is used to provide essential public services to communities and forms part of the municipality's service delivery network.

INTRODUCTION: ASSETS

Some of the typical characteristics of infrastructure assets are as follows:

- they are part of a network or system,
- they are specialised in nature and not easily replaced,
- they are immovable,
- they have long useful lives,
- they are primarily used to provide services rather than generate profits
- they may be subject to constraints on disposal

Why Infrastructure Assets Require Strong Controls

Infrastructure assets represent a significant portion of a municipality's asset base and are critical for service delivery. Effective controls should include:

- Accurate asset registration/ identification
- Asset componentization
- Regular condition assessments
- Preventative maintenance
- Physical verification,
- Monitoring of capital projects,
- Timely replacement and renewal planning

INTRODUCTION: ASSETS

Weak controls over infrastructure assets can result in:

- Service delivery failures
- Asset impairments
- Financial losses
- Material misstatements in the Annual Financial Statements
- Potential Material Irregularities identified by the AGSA

INTERNAL CONTROLS

- **Internal controls** are the policies, procedures, systems, and activities put in place by management to provide reasonable assurance that an organisation achieves its **objectives**, **safeguards its assets, produces reliable financial information** and **complies** with applicable laws and regulations

- Controls are put in place in a bid to reduce operational and financial risks, including reporting risks.

Benefits of Internal Controls
- Promote the economical and efficient use of municipal resources,
- Promote accountability and prevent theft, loss, damage, or misuse of municipal assets,
- Ensure the integrity of financial reporting and accounting information,
- Promote adherence to legislation, regulations, policies and procedures,

INTERNAL CONTROLS

Internal controls are broadly divided into two:-

- Preventative controls
- Detective controls

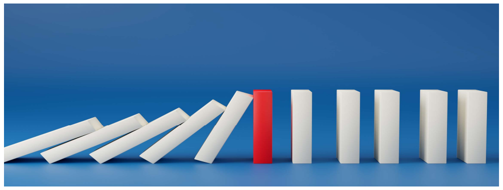
- **Preventative controls** - aim to deter errors or fraud from happening in the first place and include thorough documentation and authorization practices. They are proactive measures implemented by management to reduce risk before any problem arises.
- **Detective controls** - are backup procedures (not preventative) that are designed to identify errors, irregularities, fraud, theft, or non-compliance after they have occurred, so that corrective action can be taken promptly,

INTERNAL CONTROLS

Internal controls are the **policies**, **procedures**, **systems**, and **activities** put in place by management to provide reasonable assurance that an organisation achieves its objectives and goals.

Examples of **Internal Controls** that generally management should put in place to ensure effective use of municipal resources:

- Physical Controls/ Safeguarding of Municipal Assets,
- Segregation of duties between officials,
- Monthly reconciliations,
- Keep proper records of assets and perform conditional assessments
- Asset tagging and maintenance of asset registers,
- Management review of financial reports,
- Policies and Procedures



KEY CONTROLS: ASSET MANAGEMENT CYCLE

Physical Controls/ Safeguarding of Assets

Physical controls are measures implemented by management to protect municipal assets from theft, loss, misuse, damage, vandalism, or unauthorised access. The custody controls should include procedures that specify how assets need to be stored, secured, treated and maintained. These controls ensure that assets remain available and in good condition to support service delivery.

The controls are designed to:-

- Protect municipal assets from theft and loss
- Prevent unauthorised use of assets
- Safeguard public resources
- Ensure assets remain available for service delivery
- Promote accountability for assets
- Reduce the risk of financial losses and Material Irregularities.

The **records** of the assets in the custody of the municipality need to be kept up to date to enable safeguarding and control over the appropriate use of these assets.

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Physical Controls/ Safeguarding of Assets

Recording of New Assets - All new assets should be recorded in a register at the point of acquisition and physical counts should be performed on a regular basis to confirm and ensure that the register accurately and completely reflects the physical assets owned and controlled by the institution

Assets Maintenance Plan - Based on the conditional assessments of assets, a maintenance plan specifying when and how often which assets will be maintained should be established. The maintenance plan should be used to inform the budget of the institution, to ensure that funds will be available for maintenance when required.

Assets maintenance is **critical** to ensure that capital assets continue to operate at optimal levels of effective, efficient and economical service delivery and to prevent assets from having to be replaced at great expense.

KEY CONTROLS: ASSET MANAGEMENT CYCLE

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Segregation of duties between officials

Segregation of duties (SoD) is an internal control that requires key asset management functions and responsibilities to be divided among different officials to ensure that no single individual has complete control over an asset transaction from initiation to completion. The institution's policies and procedures should include clear controls which will be implemented to govern the management of assets. The purpose of the control is to prevent the risk of fraud and errors and ensure accuracy of municipal assets records.

The segregation of duty as an internal controls enhances:-

- Accountability
- Transparency
- Accuracy of municipal asset records
- Reliability of financial reporting
- Compliance with legislation and policies
- Safeguarding of municipal assets

KEY ASSETS MANAGEMENT CONTROLS

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Segregation of duties between officials

The segregation of duties should be prescribed by these policies and procedures to ensure that the following functions are performed by independent individuals:

- Custody and recording of assets
- Review and reconciliation

The accuracy and completeness of the asset register should be regularly and independently reviewed by the asset manager.

A reconciliation should be performed, preferably monthly, between the asset accounting records and the asset register and any differences should be resolved by investigating the reason for the difference and making the required adjustments, authorised in terms of the delegation framework.

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Keep proper records of assets and perform conditional assessments

Maintaining **accurate** and **complete** asset records, together with regular condition assessments, is a fundamental asset management control that supports accountability, reliable financial reporting, effective maintenance planning, and sustainable service delivery.

Maintaining Proper Asset Records

The municipality must maintain a complete, accurate, and up-to-date Asset Register and Minor Assets Register that contain, at a minimum:

- Asset description and classification
- Unique asset identification number
- Acquisition date
- Cost or fair value
- Funding source
- Location of the asset
- Responsible custodian
- Useful life and residual value
- Depreciation and Accumulated depreciation and carrying values
- Asset condition and status
- Disposal information, where applicable

KEY ASSETS MANAGEMENT CONTROLS

Keep proper records of assets and perform conditional assessments

Asset records must be updated promptly for all additions, transfers, impairments, revaluations and disposals, and must be supported by appropriate and credible source documentation.

Control Objective: To ensure the completeness, existence, accuracy, and valuation of municipal assets and to support reliable financial reporting in accordance with GRAP Standards.

Asset Condition Assessments: The municipality must conduct periodic condition assessments of assets, particularly infrastructure and high-value assets, to determine their physical condition, remaining useful life, maintenance requirements, and risk of failure.

Condition assessments should evaluate: Physical state of the asset, operational efficiency and functionality, level of deterioration, maintenance requirements, remaining useful life and risk of service interruption or failure.

Assets should be classified according to the condition ratings in the FAR (example: Excellent = 5 Rating (New or near new condition), Good = 4 rating (Minor wear and tear), Fair = 3 Rating (Moderate deterioration requiring maintenance), Poor = 2 Rating (Significant deterioration requiring rehabilitation) and Very poor = 1 Rating (Asset nearing failure or replacement).

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Keep proper records of assets and perform conditional assessments

Assessment results should be documented and used to:

- Inform maintenance plans and budgets
- Support impairment assessments
- Identify renewal and replacement requirements
- Prioritise capital investment decisions
- Support long-term asset management planning

Maintaining proper records and conducting condition assessments help prevent:

- Missing or unrecorded assets
- Material misstatements in the Annual Financial Statements
- Incorrect useful lives and depreciation calculations
- Asset impairments being identified too late
- Infrastructure failures and service delivery interruptions
- Unplanned maintenance and replacement costs
- Material Irregularities arising from poor asset management

KEY ASSETS MANAGEMENT CONTROLS

Asset tagging and maintenance of asset registers

Asset tagging and the maintenance of asset register - are key asset management controls that ensure municipal assets are properly identified, tracked, safeguarded, and accounted for throughout their useful lives.

Control Objective
To ensure that every movable municipal asset can be uniquely identified and traced to the responsible custodian and asset record/ FAR.

Asset tagging enables the municipality to:

- Uniquely identify each asset
- Link physical assets to the Asset Register
- Facilitate asset tracking and verification
- Enhance accountability for assets
- Reduce the risk of theft, loss, or misappropriation
- Improve the accuracy of asset records

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Management review of financial reports

Management review of financial reports is a key detective control whereby management regularly examines financial and operational reports to identify errors, unusual transactions, non-compliance, financial risks, and control weaknesses, and to ensure the accuracy and completeness of financial information.

Management review assists in ensuring that financial information is reliable, assets are properly accounted for, and corrective action is taken where deficiencies are identified.

Management reviews are conducted to:

- Assess the accuracy and completeness of financial information
- Monitor budget performance and expenditure trends
- Identify unusual or irregular transactions
- Verify the accuracy of asset-related balances and disclosures
- Ensure compliance with legislative and accounting requirements
- Detect control deficiencies and emerging risks
- Facilitate timely corrective action.

Control objective: to ensure that asset balances are corrected timely, Financial statements remain accurate and potential audit findings are avoided/ eliminated.

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Policies and Procedures

Policies and procedures are fundamental preventive controls that provide a structured framework for managing municipal assets consistently, efficiently, and in compliance with applicable legislation and accounting standards. Policies establish the principles, rules, and expectations for asset management, while procedures provide detailed guidance on how those policies must be implemented in practice.

The policy should not merely focus on accounting requirements. It should also address the **full asset lifecycle**, governance, internal controls, responsibilities, compliance, safeguarding, maintenance, verification, reporting, and disposal of assets including treatment of **minor assets**.

The municipality must establish and maintain approved asset management policies and procedures to:

- Promote sound governance and accountability
- Ensure compliance with legislative requirements
- Standardise asset management practices across departments
- Safeguard municipal assets
- Support reliable financial reporting
- Reduce the risk of fraud, errors, losses, and Material Irregularities.

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Policies and Procedures

Example of headings that should be included in a good structured Asset management policy:

- Definitions and abbreviations
- Objective of the asset management policy
- Role of the accounting officer
- Classification and identification of PPE
- Capitalization criteria
- Categorisation of the assets
- Calculation of capitalization cost of assets
- Residual values
- Depreciation of assets
- Impairment assessment
- Asset risk management
- Maintenance of assets

❑ Some of the key headings are just nice on paper, but if not implemented they have far reaching consequences. (Some of the items listed above are nicely written in the Asset Management Policies but are mostly not being implemented properly.)

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Policies and Procedures

The depreciation method applied to an asset must reflect the pattern in which the asset's future economic benefits or service potential are expected to be consumed by the municipality over its useful life. The municipality should ensure that the depreciation method selected is appropriate to the nature and usage of the asset and is applied consistently.

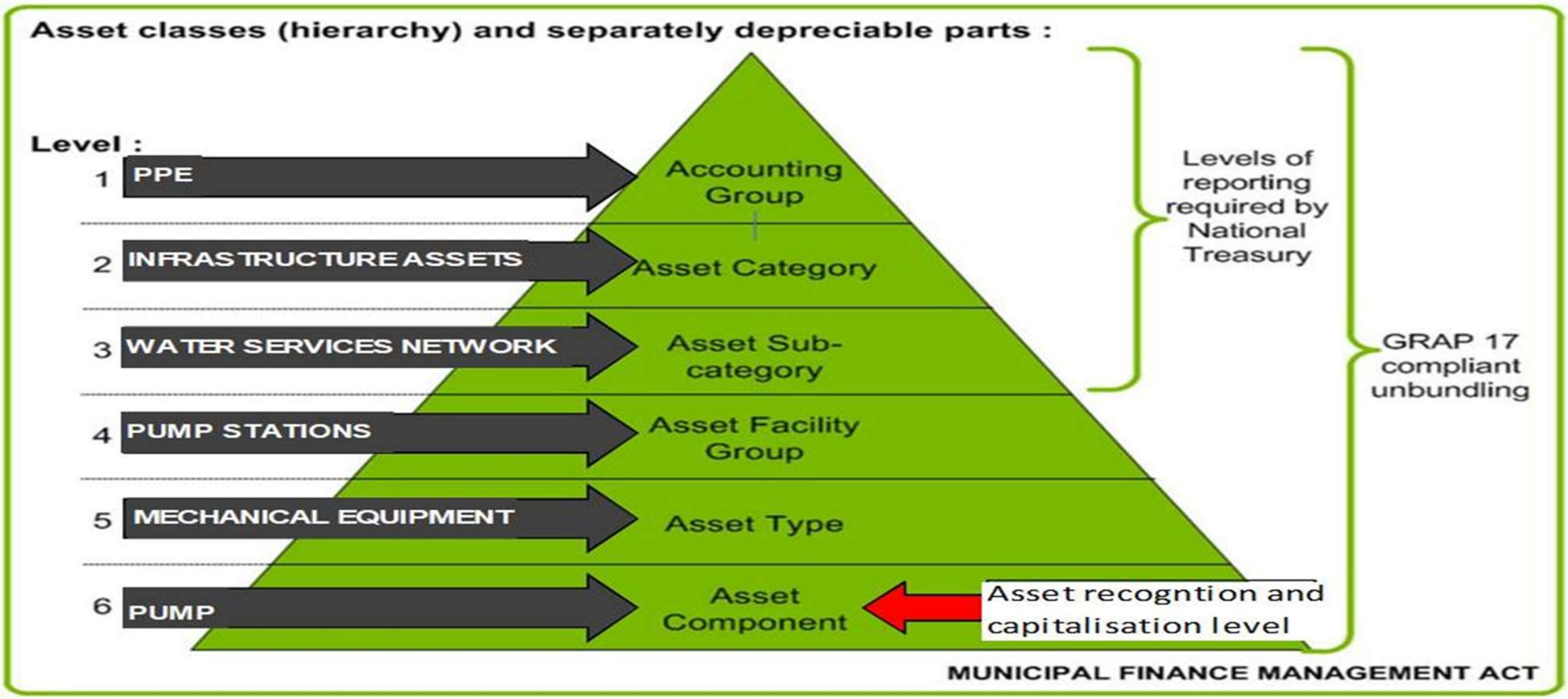
Useful lives should be consistent with the GRAP standards, accounting policies appearing on the face of the financial statements and also the National treasury guidelines.

At each reporting date, management should review the useful life, residual value, and depreciation method of all material asset classes to determine whether the assumptions remain appropriate. The review should consider the following factors:-

- Asset's physical condition,
- Maintenance history,
- Usage patterns,
- Technological changes,
- Operational requirements,
- Condition assessment results.

KEY CONTROLS: ASSET MANAGEMENT CYCLE

Categorisation of Assets in the Policy: Assets Class Hierarchy



MATERIAL IRREGULARITIES (MIs)

Material irregularity (MI) definition and Purpose

Any **non-compliance** with, or **contravention** of legislation, **fraud**, **theft** or a **breach of a fiduciary duty** identified during an audit performed under the Public Audit Act that **resulted in or is likely** to result in a **material financial loss**, the **misuse or loss** of a **material public resource**, or **substantial harm** to a **public sector institution** or the **general public.**

The purpose of Material Irregularity is to:-

- Instill a culture of accountability,
- Improve the protection of resources,
- Enhance public sector performance and encourage an ethical culture,
- Strengthen public sector institutions to better serve the people of South Africa,

ACTIVITIES THAT INCREASE THE RISK OF MATERIAL IRREGULARITIES

Common cause of material irregularity

Material Irregularities seldom occur because of a single event. They are often the result of **multiple control failures** which significantly increase the risk of Material Irregularities that would result in financial losses, audit findings, and service delivery failures. The following are the **common activities** that may lead to Material Irregularities:-

- Failure to maintain complete and accurate asset registers
- Failure to conduct regular physical verification of assets
- Inadequate safeguarding and security of assets
- Unauthorised or poorly controlled asset disposals
- Poor maintenance and asset management practices
- Failure to perform condition assessments and useful life reviews
- Weak segregation of duties and lack of independent oversight
- Inadequate management review of financial and asset reports
- Non-compliance with policies, procedures, and legislation
- Failure to investigate and address asset losses, theft, and damage
- Poor record keeping and insufficient supporting documentation
- Weak controls over minor assets
- Inadequate monitoring of capital projects and work-in-progress

AUDIT OUTCOMES AND ACCOUNTABILITY

- Audit outcomes are a reflection of the effectiveness of a municipality's governance, financial management, internal controls, and accountability processes.
- Strong accountability and effective asset management controls contribute to improved audit outcomes, while weak controls often result in audit findings, material misstatements, financial losses, and Material Irregularities.
- Positive audit outcomes are achieved when management and officials take accountability for municipal assets, maintain effective internal controls, ensure compliance with legislation and accounting standards, and promptly address identified weaknesses.
- Accountability is the foundation of good governance, sound asset management, and sustainable service delivery. The effective management of municipal assets requires clear roles, responsibilities, and accountability across all levels of the municipality.

QUESTIONS & ANSWERS

Thank You!

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