



THABA CHWEU LOCAL MUNICIPALITY

RISK APPETITE AND TOLERANCE FRAMEWORK

2022/ 2023

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1. INTRODUCTION

A Risk Appetite statement defines the thresholds of acceptable risks. This document is critical for successful risk management and facilitates effective decision-making and strategic alignment of project-level decisions with organizational strategy.

A Risk Tolerance statement states that it is not always efficient or possible to manage risks to zero residual risk or a very low residual risk threshold because of the time, cost and effort that will be required. On the other hand, it is also poor management practice to accept risks which create unnecessary exposure for the Institution.

Given the aforementioned dynamics it is important for the Institution to make an informed decision on the amount of risk the Institution is capable of bearing as part of normal management practice. This level of acceptable risk is known as a "tolerated risk or tolerance level" and establishes the benchmark for the Institution's risk tolerance. This differs from risk appetite which is the amount of residual risk that an Institution is willing accept. Risk appetite differs from Institution to Institution and can equally differ in terms of various categories of risk an Institution may face at a point in time.

The aim of defining risk tolerance is to get people to think effectively about risk when they make important decisions. Performance management systems encourage officials to think about targets and rewards for meeting them. However, the systems should equally tell officials about the amount of risk the institution can take. In essence, effective risk taking that is aligned to overall Institutional strategy should be a core skill and competency.

Tolerance levels may vary by context and are influenced by the following:

- Ability and willingness of the Accounting Officer / Authority to take and manage risks;
- Size and type of Institution;
- Skills and experience of officials;
- Maturity and sophistication of risk management processes and control environments;
- The current level of an Institution's performance; and
- Financial strength of the Institution and its ability to withstand shocks.

After all risks have been identified as well as root causes and possible consequences established, all risks should be rated to identify the High, Medium and Low risk areas in our Strategic Risks, Fraud Risks, ICT Risks and Operational Risks. The reasons why risks are rated, is to:

1.1. Allow the Municipality to use its scarce resources to focus on mitigating the more important risks.

1.2. Allow the Municipality to identify those risks that if not mitigated, may result in the institution not reaching one or more of its strategic objectives.

1.3. Allow the Municipality to identify those risks that if not mitigated, may result in the destruction of the institution.

To rate all risks, the risk rating tables as well as the risk tolerance tables are being utilized. The challenge however is that the above-mentioned tables allow for a huge amount of subjective opinion.

This leads us to the following questions:

- How can the amount of subjective opinion in the rating of risks be minimized?
- How can the amount of subjective opinion in the establishing of tolerance levels be minimized?

The instrument that can be utilized to minimize subjective opinion is to establish the risk appetite, with regard to every strategic objective of the municipality. If the risk appetite of every strategic objective is established; it means that the risk becomes unacceptable and

2. DEFINITION OF KEY CONCEPTS

2.1 RISK APPETITE

The COSO ERM Framework defines risk appetite as “the amount of risk, on a broad level, an organization is willing to accept in pursuit of stakeholder value”. Therefore, Risk Appetite deals with the pursuit of risk (upside risk) – “the amount and type of risk that an organisation is willing to pursue or retain” (ISO Guide 73).

An organisation's Risk Appetite is communicated via a Risk Appetite statement which has no fixed / defined format. The statement should include a range of quantifiable values defining the acceptable levels of risk that Thaba Chweu is willing to accept in pursuing the risks required to take in order to meet its objectives.

2.2 RISK TOLERANCE

As per the COSO Framework, risk tolerance is the degree, amount, or volume of the risk that an organization or individual will withstand. Risk tolerance tells you how sensitive the organization or people are to risks. High tolerance means people are willing to take a high risk, and low tolerance means people are not willing to take much risk. It is the willingness of a group of people or organization to accept or avoid risk. It shows the risk attitude of stakeholders or an organization in measurable units.

3. RISK APPETITE AND TOLERANCE STATEMENT FOR THABA CHWEU LOCAL MUNICIPALITY.

Risk appetite is the level of risk Thaba Chweu Local Municipality is prepared to tolerate or accept in the pursuit of our strategic objectives. Our main objective is to consider all options to respond to risk appropriately and make informed decisions that are most likely to result in sustainable service delivery and economic development through good governance.

The acceptance of risk is subject to ensuring that all potential benefits and risks are fully understood and that appropriate measures to mitigate risks are established before decisions are made. We recognise that the appetite for risk will vary according to the activity undertaken and hence different appetites and tolerances to risk apply.

It is advisable to determine and communicate the level of unexpected losses that the Institution is willing to accept in the event the risk materializes. Zero tolerance risk exposures such as fraud and corruption, regulatory compliance and health safety should be communicated to all officials.

As management decisions are informed by targets being pursued, there should be a mechanism in place that enables tracking of numbers involved to ensure that tolerance guidelines are complied with or applied as specified. This may require management to determine key risk indicators that will be utilised to monitor the risks' occurrence.

There is no "one-size fits all" approach to establishing the right risk tolerance levels. Practices will differ amongst Institutions based on the maturity of the risk management practice, available data, management expertise, sector specific dynamics and other pertinent factors. Thus, it is advisable to rather follow certain guiding principle rather than "hard and fast" rules.

This document is part of the Risk Management Framework of the Municipality and must be read in conjunction with the following documents:

- 1) Risk Management Policy
- 2) Fraud Prevention Plan and Strategy
- 3) Fraud Prevention Policy
- 4) Risk Management Strategy
- 5) Risk Management implementation plan
- 6) Risk Management and Fraud Prevention Committee Charter
- 7) Whistle blowing policy

4. BENEFITS OF A RISK APPETITE FRAMEWORK

According to COSO the following benefits flow from an effective risk appetite framework:

- It is strategic and is related to the pursuit of organizational objectives;
- Forms an integral part of corporate governance;
- Guides the allocation of resources;
- Guides the municipality's infrastructure, supporting its activities related to recognizing, assessing, responding to, and monitoring risks in pursuit of Organizational objectives;
- Influences the municipality's attitudes towards risk;
- Is multi-dimensional, including when applied to the pursuit of value in the short term and the longer term of the strategic planning cycle; and
- Requires effective monitoring of the risk itself and of the municipality's continuing risk appetite; and
- Enhanced risk management strategy decisions through quantification of risk appetite.

5. OBJECTIVES OF A RISK APPETITE FRAMEWORK

The objective of a framework is to help management make informed decisions and includes:

- Establish a process for communicating the Risk Appetite Framework across and within the municipality;
- Be driven by both top-down and bottom-up involvement of management at all levels, and embedded and understood across the municipality;
- Facilitate embedding risk appetite into the municipality's risk culture;
- Evaluate opportunities for appropriate risk taking and act as a defence against excessive risk-taking.
- Allow for the risk appetite statement to be used as a tool to promote robust discussions on risk and as a basis upon which risk management and internal audit

functions can effectively and credibly debate and challenge management recommendations and decisions;

- Be adaptable to changing business and market conditions so that, subject to approval by senior management and Council as appropriate, opportunities that require an increase in the risk limit could be met while remaining within the agreed municipal wide risk appetite;
- Cover activities, operations and systems of the Municipality that fall within its risk landscape but are outside its direct control, including suppliers; and
- Be consistent with the principles in this document.

6. MUNICIPALITY STRATEGIC OBJECTIVES

Thaba Chweu Local Municipality has the following strategic objectives:

- SO1- Provide access to quality services in line with council mandate
- SO2- Realisation of harmonious development within the municipal jurisdiction
- SO3- Increase revenue base and financial viability
- SO4- Enhance economic development & growth
- SO5- Improve institutional transformation and resources management
- SO6- Ensure effective and good governance
- SO7- Mainstreaming of social advocacy and marginalised groups
- SO8- Strengthen IGR & stakeholder relation.

7. RISK APPETITE PER STRATEGIC OBJECTIVE:

7.1 PROVIDE ACCESS TO QUALITY SERVICES IN LINE WITH COUNCIL MANDATE.

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When it takes longer than 2 months to adjudicate tenders for the provision of infrastructure;
- When capital projects are not successfully completed within the prescribed time period;
- When capital projects are being regularly postponed;
- When infrastructure projects are not completed within the quality control parameters as stipulated in the service level agreement;
- When more than 10% of the funds allocated for capital projects (Grants included) are unspent;
- When there's inexperienced and incompetent technical personnel to manage infrastructure projects properly;
- When critical infrastructure is not maintained within the prescribed time period as stipulated;
- When maintenance plans are not developed and reviewed within prescribed period;

- When critical infrastructure is being damaged/vandalised to a point where service delivery is compromised;
- When critical infrastructure is being tampered with by an unauthorised person
- When water and electricity losses are unaccounted for;

7.2 REALISATION OF HARMONIOUS DEVELOPMENT WITHIN THE MUNICIPAL JURISDICTION

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When there are no new residential developments to cater for the needs of the community;
- When environmental damage occurs without any steps to rehabilitate the situation;
- When controls to prevent possible environmental damage is not function;
- When the Municipality does not have proper capacity to enforce relevant legislation/by-laws to ensure a clean and healthy environment.

7.3 INCREASE REVENUE BASE AND FINANCIAL VIABILITY

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When the Municipality cannot service the ESKOM debt
- When a Municipality fails to pay within 30 days
- When Information technology system is not secured
- When there's no rotation of suppliers;
- When incorrect billing is performed;
- Continuous reduction in municipal revenue;
- Inability to perform additional activities and related services that generate municipal revenue;
- Postponing of capital projects and municipal services due to shortage of cash
- When community members are not paying for services rendered
- Requesting bail out /additional funding from National Treasury
- When Municipality fails to comply with all laws and regulations of the municipality;
- When grants are used to pay for operational expenditures;
- When there's no business continuity;
- When there's no customer satisfaction model;
- Prolonged supply chain processes;
- When the audit action plan targets are not achieved within prescribed timeframes;
- When a Municipality is dependent on an overdraft.
- Irregular and fruitless expenditure of more than R1M in one financial year.

7.4 ENHANCE ECONOMIC DEVELOPMENT & GROWTH

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When local economic growth rate is lower than the average set;
- When private enterprise finds it difficult to establish businesses within Thaba Chweu
- When the Municipality is unable to attract investors of certain kinds
- Inability to promote local economic development
- Inability to reduce unemployment targeted rate
- When the local economic development strategy is outdated or not implemented.
- When more than the average amount of businesses is closing per month
- When more businesses are closing per month than new ones established.

7.5 IMPROVE INSTITUTIONAL TRANSFORMATION AND RESOURCES MANAGEMENT

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When human resource budget is more than 35%
- When labour issues are not addressed
- When disciplinary structure is not functional
- When Municipality does not have proper capacity to enforce its own by-laws
- Low staff morale
- When 15% of specialized positions are not being filled.
- Outdated delegated powers of administrative office bearers.
- Outdated Governance Model and delegations for political office bearers.
- 15% of internal controls not implemented.
- Outdated by-laws
- Outdated policies
- Disciplinary system not implemented.
- Organizational structure outdated.
- Non-functional occupational health and safety systems.

7.6 ENSURE EFFECTIVE AND GOOD GOVERNANCE

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When council resolutions are not implemented
- Organisational structure is not aligned with the strategic objectives of the municipality.
- When there are no By-Laws
- Outdated policies
- Lack of business continuity
- Lack of clear roles & responsibilities
- Ineffective & non-functional occupational health and safety
- 10% increase in occupational health and safety incidents/accidents.
- Lack of accountability

- Non reporting of fraud; theft & corruption.

7.7 MAINSTREAMING OF SOCIAL ADVOCACY AND MARGINALISED GROUPS

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When social amenities are dilapidated and not maintained within the prescribed period
- When social amenities are being damaged/vandalised to a point where service delivery is compromised
- When equipment is being damaged or stolen to a point where new equipment cannot be provided by the municipality.
- When new projects on social amenities are not provided.
- When there is none compliance to the Employment Equity Act and Labour relations Act Marginalised groups (people with disabilities)
- When there is an increase on woman and child abuse (GBV)
- When there is an increase in number of drugs and substances abuse
- When there is an increase in Covid-19 cases

7.8 STRENGTHEN IGR & STAKEHOLDER RELATIONS.

The following gives an indication of a threshold and if crossed, it will be necessary to allocate resources such as time; money, personnel and equipment to mitigate risk:

- When the Municipality is unable to fully implement Batho-Pele Principle; Service Standards & Operational Vuka Sisebenze
- When there's lack of coordination between Stakeholders

8. CONCLUSION

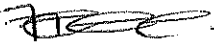


Greater understanding of risk and the risks being faced by the Municipality is a powerful tool for aligning stakeholder interests and ultimately giving the Municipality the best chance of achieving its strategic goals and objectives. The Risk appetite will allow the Municipality to focus on scarce resources to successfully mitigate all risks that have become a reality and might jeopardise municipal service delivery.

The process of identification, rating and mitigating of enterprise risks, allows the Municipality to use risk intelligence as a management resource, to prevent occurrences that might prevent the institution from reaching its strategic objectives. This process will enable the Municipality to avoid the situation where risk will end up driving its strategy.

9. RISK APPETITE REVIEW

An Institution's Risk Appetite and Tolerance should be reviewed annually to align it to new circumstances and together with the Institution's targets and available resources to determine the Institution's risk bearing capacity.

10. APPROVAL

1. Compiled by  11/04/2022
Risk Management Unit: Date
2. Recommended by  21/04/2022
Chairperson RMFPC Date
3. Approved by  21/04/2022
Municipal Manager Date

11. ROLES AND RESPONSIBILITIES

The people responsible for risk appetite can be categorized into four distinct categories, namely implementers, support function, oversight and assurance providers.

1. IMPLEMENTERS

1.1 The Accounting Officer (Municipal Manager)

The Municipal Manager is ultimately responsible for risk management within the municipality. The Municipal Manager is accountable to the Council regarding the effectiveness of the risk management process. By setting the tone at the top, the Municipal Manager promotes accountability, integrity and other factors that create a positive control environment.

The roles of the Municipal Manager relating to the risk appetite include the following:

- establish an appropriate risk appetite for the Municipality (in collaboration with the CRO) which is consistent with the municipality's short- and long-term strategy, business and capital plans and risk capacity;
- be accountable, together with the CRO and managers for the integrity of the Risk Appetite Framework, including the timely identification and escalation of breaches in risk limits and of material risk exposures;
- ensure, in conjunction with the CRO, that the risk appetite is appropriately translated into risk limits for strategic and financial planning, decision-making processes and compensation decisions;
- ensure that the municipality's wide risk appetite statement is implemented by management;
- provide leadership in communicating risk appetite to internal and external stakeholders so as to help embed appropriate risk taking into the municipality's risk culture;
- set the proper tone and example by empowering and supporting the CRO in his/her responsibilities, and effectively incorporating risk appetite into the municipality's decision-making processes;
- ensure managers have appropriate processes in place to effectively identify, measure, monitor and report on the risk profile relative to established risk limits on a continual basis;
- dedicate sufficient resources and expertise to risk management, internal audit and IT infrastructure to help provide effective oversight of adherence to the framework;
- act in a timely manner to ensure effective management, and where necessary mitigation, of material risk exposures, in particular those that are close to or exceed the approved risk appetite statement and/or risk limits; and
- notifying Risk Management Committee and the Council of serious breaches of risk limits and unexpected material risk exposures.

1.2 Management

Management at all levels within the Municipality owns the risks, thus in taking that ownership they also accountable to the Municipal Manager for integrating the principles of risk management into their daily routines to enhance the achievement of their service delivery objectives.

In discharging their high-level responsibilities relating to risk appetite, management:

- ensure alignment between the approved risk appetite and planning, compensation, and decision-making processes of the municipality;
- embed the risk appetite statement and risk limits into management's activities so as to embed prudent risk taking into the municipality's risk culture and day to day management of risk;
- establish and actively monitor adherence to approved risk limits;
- implement controls and processes to be able to effectively identify, monitor and report against allocated risk limits;
- act in a timely manner to ensure effective management, and where necessary, mitigation of material risk exposures, in particular those that exceed or have the potential to exceed the approved risk appetite and/or risk limits; and
- escalate promptly breaches in risk limits and material risk exposures to the CRO and senior management in a timely manner.

2. RISK MANAGEMENT SUPPORT

2.1 Chief Risk Officer (CRO)

Accountability for risk management in the Municipality is assigned to the Accounting Officer (Municipal Manager) and is sub-delegated to the CRO to facilitate and coordinate the development and implementation of risk.

The CRO provides specialist expertise in providing a comprehensive support service to ensure systematic, uniform and effective enterprise risk management. The CRO plays a vital communication link between operational level, management, senior management, risk management committee and other relevant committees. High level responsibilities to achieve this include:

- develop an appropriate risk appetite for the Municipality to meet its needs;
- obtain Council's approval of the developed risk appetite and regularly report to Council on the municipality's risk profile relative to risk appetite;
- actively monitor the municipality's risk profile relative to its risk appetite, strategy and risk capacity;
- establish a process for reporting on risk and on alignment (or otherwise) of risk appetite and risk profile with the municipality's risk culture;
- ensure the integrity of risk measurement techniques and information systems that are used to monitor the municipality's risk profile relative to its risk appetite;
- establish and approve appropriate risk limits for the Municipality that are consistent with the municipality's risk appetite statement;
- independently monitor the municipality's risk limits aggregate risk profile to ensure they remain consistent with the municipality's risk appetite;
- act in a timely manner to ensure effective management, and where necessary mitigation, of material risk exposures, in particular those that are close to or exceed the approved risk appetite and/or risk limits; and
- escalate promptly to Council and the Accounting Officer any material risk limit breach that places the Municipality at risk of exceeding its risk appetite, and in particular, of putting in danger the financial condition of the municipality.

3. RISK MANAGEMENT OVERSIGHT

3.1 Council

Council is responsible for overseeing the complete spectrum of governance within Thaba Chweu Local Municipality.

This responsibility would therefore also include:

- approve the municipality's Risk Appetite Framework and ensure it remains consistent with the municipality's short- and long-term strategy, business and capital plans, risk capacity as well as compensation programs;
- hold the Accounting Officer and management accountable for the integrity of the framework, including the timely identification, management and escalation of breaches in risk limits and of material risk exposures;
- discuss and monitor to ensure appropriate action is taken regarding "breaches" in risk limits;
- question management regarding activities outside the Council-approved risk appetite statement, if any;
- obtain an independent assessment (through internal assessors, third parties or both) of the design and effectiveness of the framework and its alignment with supervisory expectations;
- satisfy itself that there are mechanisms in place to ensure management can act in a timely manner to effectively manage, and where necessary mitigate, material adverse risk exposures, in particular those that are close to or exceed the approved risk appetite statement or risk limits;
- ensure adequate resources and expertise are dedicated to risk management as well as internal audit in order to provide independent assurances to Council and management that they are operating within the approved framework, including the use of third parties to supplement existing resources where appropriate; and
- ensure risk management is supported by adequate and robust information system to enable identification, measurement, assessment and reporting of risk in a timely and accurate manner.

3.2 Risk Management and Fraud Prevention Committee

In discharging its oversight responsibilities relating to the risk appetite framework:

- ensure that the risk appetite framework is approved by the Council;
- evaluate the effectiveness of mitigating strategies implemented to address the material risks of the Municipality (treatment action plans);
- ensure that the committee is informed of all changes to the risk management strategy, implementation plan, policy and framework;
- review and monitor the effectiveness of risk control systems, the reliability and accuracy of risk management reporting and fraud prevention plan;
- review any material findings and recommendations by assurance providers on the system of risk management and monitor that appropriate action is instituted to address the identified weaknesses; and
- provide guidance to the CRO and other relevant risk management stakeholders on how to manage risks within the risk appetite level;

4. RISK MANAGEMENT ASSURANCE PROVIDERS

4.1 Internal Audit

Internal Audit is responsible for providing independent assurance on the effectiveness of risk management, controls and governance processes, as designed and represented by management, are adequate and function in a manner to ensure that amongst other things risks are appropriately identified and managed, based on the scope of their coverage plan. Responsibilities of Internal Audit in the risk appetite process include:

- routinely include assessments of the Risk Appetite Framework on a municipal basis;
- identify whether breaches in risk limits are being appropriately identified, escalated and reported, and report on the implementation of the framework to the Audit Committee and Council as appropriate;
- independently assess periodically the design and effectiveness of the framework and its alignment with management expectations;
- assess the effectiveness of the implementation of the framework, including linkage to organisational culture, as well as strategic and business planning, compensation, and decision-making processes;
- assess the design and effectiveness of risk measurement techniques and information systems used to monitor the municipality's risk profile in relation to its risk appetite.
- report any material deficiencies in the risk appetite framework and on alignment of risk appetite and risk profile with risk culture to Council, Audit Committee and management in a timely manner; and
- evaluate the need to supplement its own independent assessment with expertise from third parties to provide a comprehensive independent view of the effectiveness of the risk appetite framework.