



Presented To:	Audit Committee
Presented:	Tuesday, Oct 04, 2016
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Type:	Managers' Reports

Request for Decision

Proposed Revisions to the Auditor General's Office and Audit Committee

Resolution

See the enclosed report.

Signed By

Auditor General
Ron Foster
Auditor General
Digitally Signed Sep 19, 16

Request for Decision on Proposed Revisions to the Auditor General’s Office and Audit Committee

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Resolution

THAT the report from the Auditor General dated September 19, 2016 regarding proposed changes to the audit planning process, audit protocols, performance metrics and performance monitoring process for the Auditor General’s Office be approved and recommended to Council;

That the introduction of an Enterprise Risk Management process within CGS be recommended to Council;

That the proposed amendments to the mandate and composition of the Audit Committee be recommended to Council; and

That, subject to the approval of Council, staff be directed to prepare the necessary changes to the Procedure By-law and By-law 2015-217.

Background

In 2013, James Key from the Shenandoah Group, LLP was engaged by Council to re-evaluate the audit approach and to enhance audit committee oversight of the audit activity in CGS. According to the Shenandoah Report:

“Most governance oversight boards or councils establish an audit committee to oversee the governance monitoring function. Internal auditors, external auditors, and other assurance providers are usually accountable to the audit committee. This oversight role requires an audit committee knowledgeable about strategic, operational, financial, and compliance risks and the regulatory and best practices that inform those risks. With a new council grounded in good governance, risk management, and audit oversight principles, stakeholders will be assured the city resources will be managed more efficiently and more effectively toward CGS’ objectives.”

Recommendations from the Shenandoah Report

To enhance audit committee oversight, the Shenandoah Report recommended that:

1. The CGS Audit Committee examine other audit services that would provide more value, e.g. financial (without attestation), consulting, compliance assurance, operational assurance in addition to the mostly value-for-money activity currently being done. Research suggests that AG’s Office develop an annual audit plan that is broader than value-for-money audits.

2. The CGS Audit Committee establish and enforce a protocol that ensures management is engaged by the AG's Office during the annual risk assessment and audit plan cycle to offer management's view of risk. Moreover, the protocol should establish a specific time frame for management to agree with the facts or bring forward new information. The protocol should then allow for management's plan to resolve or mitigate the observations. Only then would a "final draft" be presented to council in public session.
3. The CGS Audit Committee work with the OAG to establish performance metrics for the AG's Office. They might include such measures as audits planned vs. completed and money recovered vs. hypothetical savings.
4. Network with the AG Offices in other municipalities to assess resourcing models, budgeting levels and maturity expectations appropriate to the needs of CGS.
5. Develop an Enterprise Risk Management (ERM) process that considers all risk across organizational silos and which maps to the CGS' strategic plan. Once implemented, an effective ERM process will provide better input to strategic planning, annual business planning, business continuity planning, and disaster recovery planning. Such an ERM process would also form a baseline for the AG's Office to develop a risk assessment and risk-based audit plan that will better provide assurance services to CGS.
6. Develop an Audit Committee Charter with bylaws that require two independent committee members with audit and financial expertise.
7. The CGS Audit Committee determine the level of funding appropriate for the audit services required to adequately assure risk.

Implementation Plan for Recommendations

In response to the Shenandoah Report recommendations, the following is a suggested action plan that has been prepared for the review and approval of Audit Committee and Council:

1. Examine other audit services

The AG's Office engaged members of Audit Committee and Council when preparing the audit plan for 2016 to ensure its audit services responded to the needs of Council.

Proposal 1: Senior management will be engaged during the risk assessment and audit planning process in Q4 of 2017 going forward.

2. Establish and enforce a protocol for audits

The AG's Office benchmarked with the AG Offices in Toronto, Ottawa and Markham to identify relevant protocols for audits. The results are shown in Attachment 1.

Proposal 2: The following audit protocols, which have been in place since the beginning of 2016, are proposed for conducting audits:

- a) Notice to be provided one month in advance of audit;
- b) Comments on factual accuracy of findings are due two weeks after issue of draft report;
- c) Management responses are due two weeks after issue of updated draft report; and
- d) Final report to be issued one week after the closing meeting with senior staff and the Audit Committee Chair and Vice-Chair.

3. Establish performance metrics for the AG's Office

In addition to the benchmarking exercise at Attachment 1, input was obtained from the CAO, Chair & Vice-Chair of the Audit Committee on potential performance metrics for the AG's Office.

Proposal 3: The following performance metrics be used for the AG'S Office:

- a) Feedback from Annual Survey of Audit Committee Members;
- b) Feedback from Annual Survey of Senior Management;
- c) Percentage of audit plan completed;
- d) Quantity and quality of improvements recommended;
- e) Responsiveness to requests from Council and Audit Committee;
- f) Adequacy of management of budget and staff within AG's Office;
- g) Adequacy of maintenance of Wrongdoing Hotline; and
- h) Adequacy of development and maintenance of ERM process.

4. Network with other AG Offices

The AG's Office reached out to its counterparts in Toronto, Ottawa and Markham to complete the benchmarking study at Attachment 1.

Proposal 4: Performance data on the counterparts of the AG's Office will be tracked annually and used for benchmarking and performance monitoring purposes.

5. Establish an Enterprise Risk Management (ERM) process

According to the Shenandoah Report, "Enterprise Risk Management processes inform strategic planning, annual business planning and business continuity plans. They also lead to more robust business plans and more effective project management." Attachment 2 identifies other benefits of ERM processes such as a more risk focused culture and efficient use of resources.

Proposal 5: In conjunction with the City Manager, the AG's Office will develop and implement an ERM process in 2017 and 2018 including tools and training processes to identify, assess and report risks. The City Manager will take the lead on risk mitigation efforts. Costs for implementation and maintenance of the ERM process will be borne by the Auditor General's Office.

6. Revise the Mandate and Composition of Audit Committee

The Audit Committee duties are generally set out at Article 38 of our Procedure By-law 2011-235. All members of Council are currently members of the Committee. The proposed revision to the Audit Committee Mandate shown at Attachment 3 was developed with input from the Chair and Vice-Chair of the Audit Committee, Mayor, Chief Administrative Officer, City Clerk and City Solicitor.

As outlined in the attachment, the composition of the Committee would be set at a minimum of five and a maximum of seven members and would be augmented by one external advisor to ensure the committee has sufficient expertise in governance, risk management and controls during the implementation of ERM process in 2017 and 2018. The next Council can evaluate the continued need for an external advisor on Audit Committee.

As the Audit Committee will be tasked with overseeing the ERM implementation and ongoing reports on significant risks within CGS as well as the Wrongdoing Hotline, external auditors and Auditor General's Office, it is important that the members collectively have knowledge, skills and experience in auditing, accounting, finance, risk management and governance processes. Many public sector organizations, including municipalities such as Edmonton, are appointing non-voting external members or advisors to their Audit Committees to augment the skills and knowledge of committee members.

To avoid potential conflicts of interest, any external advisor appointed to the Committee would have to consent in writing to not be employed with a firm that prepares or audits the financial statements of the City, its boards, and municipally-controlled corporations and to neither be a candidate nor a member of an election campaign team.

If this approach is acceptable to Council, a subcommittee would be formed consisting of the Chair and Vice Chair of Audit Committee and the Auditor General to select an appropriate external advisor to Audit Committee with appropriate knowledge, skills and experience.

An advertisement for the external advisor for a two-year appointment to Audit Committee would be developed and posted in Q4 2016. The estimated annual cost for this external advisor in 2017 and 2018 would be \$3,000 to \$5,000 which includes \$400 per day for attendance at meetings and reimbursement of travel costs incurred in accordance with CGS policy. Per diems paid by other municipalities in Ontario range from \$100 to \$500.

Proposal 6: The Audit Committee Mandate at Attachment 3 be endorsed by Audit Committee and recommended to Council. An external advisor would be appointed in Q4 2017 for a two-year term and would be paid from the AG's Office budget in accordance with the terms and conditions outlined within this report.

7. Determine the level of funding appropriate for audit services in CGS

The minimum funding level for the AG's Office in CGS set out in By-law 2015-217 is 0.065% of the annual operating budget. To maintain the expanded audit services and to provide timely and effectively support of the wrongdoing hotline, to ensure the ERM initiative is successfully initiated and maintained, and to support the fees for an external advisor to the Audit Committee, incremental funding of \$12,500 will be required in both 2017 and 2018 to bolster the capability of the Auditor General's Office.

Increasing the capability of staff in the AG's Office is in keeping with the best practices recommended within the Shenandoah Report and is also aligned with CGS' leadership development program. It will also allow for a more effective and timely response to complaints within the Wrongdoing Hotline which and will support CGS' Strategic Plan which promotes open, transparent, accountable government.

Providing the AG's Office with additional temporary funding in 2017 and 2018 is also considerably more cost effective than increasing reliance on external contractors which might cost an additional \$50,000 to \$100,000 annually or adding a full-time position in the risk management section of the Finance Department which would cost \$100,000 or more annually.

Proposal 7: The AG's Office budget be increased by \$12,500 for 2017 and 2018 and these increases be funded from the Auditor General's Reserve. This proposed increase will be fully documented in a business case which will be presented during the 2017 budget process.

Financial Impact

Assuming a 4.0% increase in the operating budget, this resolution would result in an increase to the AG's Office budget in 2017 of \$12,500 and a regular increase of \$12,176 for growth in the annual operating budget. The incremental funding for 2017 and 2018 will not affect the tax levy as the funding source will be the Auditor General's Reserve.

Expenses	2016	2017 Base Budget	Funding from AG's Reserve	2017
Salaries and benefits	\$294,618	\$306,021		\$306,021
Materials	3,926	1,473		1,473
Professional development and training	10,487	12,500	\$12,500	25,000
Purchased contract services	23,022	24,000		24,000
Internal recoveries	21,353	21,588		21,588
Total	\$353,406	\$365,582	\$12,500	\$378,082

Benchmarking of Auditor General Functions

Attachment 1

Questions	Toronto	Ottawa	Greater Sudbury	Markham
Where does AG function report administratively?	Council through Audit Committee	Council through Audit Committee	CAO	Commissioner Corp Services
Where does AG function report functionally?	Council through Audit Committee	Council through Audit Committee	Council through Audit Committee	Council through General Committee
Are there formal terms of reference for Audit Committee?	Yes	Yes	Yes, but only very basic terms of reference	No Audit Committee
Are any external members appointed to Audit Committee?	No	No	An external member may be appointed in Q4 2016 to respond to the recommendation of James Key.	No Audit Committee
What training is provided to Council in Governance, Risk Management and Controls?	Briefings provided by staff not AG	New councilors briefed by AG on role of Audit.	Initial training in Governance was provided in orientation sessions to Council	No formal training other than familiarization of role of AG
What training is provided to Audit Committee in Governance, Risk Management and Control (GRC) Processes?	No training but Roles and Responsibilities Of AC clarified in formal report	Nothing specific	Training in GRC processes will be provided to Audit Committee members in 2016 and 2017	No Audit Committee
Does AG function have a formal mandate or charter outlining his/her responsibilities and powers?	Yes within the Municipal Code which contains City By-laws	Yes, within By-laws no. 2013-375 and 2015-11	Yes, within By-law 2015-217	Audit Charter drafted but not approved yet
Is an annual report from AG required?	Yes	Yes	Yes	No
Is an annual audit plan required?	Yes	Yes	Yes	Yes
Is an annual risk assessment required?	No, but a formal risk assessment is completed every 5 years	No but it is prepared to support the annual audit plan	No, but it is prepared to support the annual audit plan	No, but it's part of 4-year audit plan
Does the City have an Enterprise Risk Management Process?	No	Yes	No, but plans are being developed to implement ERM in 2017	No
Are the AG's reports on the City's website?	Yes	Yes	Yes	Yes
Does your office have formal protocols for				
a) Advance notice to audit entity about start date of audit?	A project start letter is sent to management prior to start	Letter sent to auditee prior to start of audit and a kick-off meeting is held	Notice to be provided one month in advance of audit	No formal protocols exist
b) Time for providing responses to draft audit report	At least 2 weeks allowed to provide comments and a preliminary response	A 4-week turn-around exists for the draft report to vet audit findings	Comments on draft report findings would be due two week after issue	No formal protocols exist
c) Time for providing responses to final audit report	At least 1 week is allowed for final response	A 4-week turn-around exists for the final report to obtain management responses	Management response would be due two weeks after issue of final report	No formal protocols exist
What performance measures are reported annually to Audit Committee or Council for AG function?	Actual dollar savings; potential savings; at risk dollars; the impact on activities with unidentifiable dollars	No formal performance measures exist	a) Percentage of audit plan completed b) Feedback from Annual Survey of Audit Committee Members c) Feedback from	No formal performance measures exist

Benchmarking of Auditor General Functions

Attachment 1

			<p>Annual Survey of Senior Management</p> <p>d) Quantity of cost savings, productivity improvements or revenue generation opportunities identified in audits</p> <p>e) Quantity and quality of improvements recommended to internal control, risk management and governance processes</p> <p>f) Responsiveness to requests from Council and Audit Committee</p> <p>g) Adequacy of management of budget and staff within AG's Office</p> <p>h) Adequacy of maintenance of Wrongdoing Hotline</p>	
<p>What is the budget for your office relative to the operating budget of the City for 2016?</p>	<p>Audit Budget: \$4.97 M</p> <p>Optg Budget: \$10.06 B</p> <p>Percent: 0.0494</p>	<p>Audit Budget: \$1.79 M</p> <p>Optg Budget: \$3.26 B</p> <p>Percent: 0.0549</p>	<p>Audit Budget: \$353 K</p> <p>Optg Budget: \$518 M</p> <p>Percent: 0.068</p>	<p>Audit Budget: \$150 K</p> <p>Optg Budget: \$186 M</p> <p>Percent: 0.081</p>

What is Enterprise Risk Management (ERM)?

ERM is a way to effectively manage risk across the organization through the use of a common risk management framework. This framework can vary widely among organizations but typically involves people, rules, and tools. This means individuals with defined responsibilities use established, repeatable processes (rules), and the appropriate level of technology (tools) to mitigate risk. A committee of five organizations dedicated to thought leadership around risk management provided a definition of ERM in 2004. The Committee of Sponsoring Organizations (COSO) defined it as:

"... a process, effected by the entity's board of directors, management, and other personnel, applied in strategy-setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within the risk appetite, to provide reasonable assurance regarding the achievement of objectives."

Benefits of Enterprise Risk Management

As business risks continue to increase, organizations are finding it necessary to implement some sort of formal risk management system. An effective enterprise risk management (ERM) program can help organizations manage their risks and maximize opportunities. Organizations in all types of industries, public and private, have observed a variety of benefits from enhancing their risk management programs.

Organizations often find that ERM programs provide a combination of both qualitative and quantitative benefits. While there are many benefits to ERM, let's focus on six of them.

Benefit one: creation of a more risk focused culture for the organization

Organizations that have implemented ERM note that increasing the focus on risk at the senior levels results in more discussion of risk at *all* levels. The resulting cultural shift allows risk to be considered more openly and breaks down silos with respect to how risk is managed.

As risk discussions develop into a standard part of the overall strategic business processes, operational units often find that addressing risk in a more formal way helps manage their part of the organization as well. Communication and discussion of risk is recognized as not only a process to provide information to senior management, but a way to share risk information within and across operations of the company, and allow better insights and decision making concerning risk at all levels.

Benefit two: standardized risk reporting to senior management and board of directors

ERM supports better structure, reporting, and analysis of risks. Standardized reports that track enterprise risks can improve the focus of directors and executives by providing data that enables better risk mitigation decisions. The variety of data (status of key risk indicators, mitigation strategies, new and emerging risks, etc.) helps leadership understand the most important risk areas. These reports can also help leaders develop a better understanding of risk appetite, risk thresholds, and risk tolerances. Reports to directors can also improve the accountability of executives for mitigating significant risks and/or realizing significant opportunities.

One of the major values of ERM risk reporting is improved, timeliness, conciseness, and flexibility of the risk data. This provides the data needed for improved decision making capabilities within the executive and director levels, and in other layers of management. ERM helps management recognize and unlock synergies by aggregating and sharing all corporate risk data and factors, and evaluating them in a consolidated format.

Benefit three: improved focus and perspective on risk

ERM develops leading indicators to help detect a potential risk event and provide an early warning. Key metrics and measurements of risk further improve the value of reporting and analysis and provide the ability to track potential changes in risk vulnerabilities or likelihood, potentially alerting organizations to changes in their risk profile.

ERM also permits a more complete viewpoint on risk. Traditional risk practices focus on mitigation, acceptance, or avoidance. However, effective ERM processes gives management a framework to evaluate risk as an opportunity to increase competitive positions and exploit certain market and operational conditions.

Benefit four: efficient use of resources

In organizations without ERM, many individuals may be involved with managing and reporting risk across operational units. While developing an ERM program does not replace the need for day to day risk management, it can improve the framework and tools used to perform the critical risk management functions in a consistent manner. Eliminating redundant processes improves efficiency by allocating the right amount of resources to mitigating the risk.

Benefit five: improved plans

Organizations that have implemented ERM and made efforts to integrate it within other key management processes reported notable improvements to the quality of plans at various levels including strategic, operational, tactical, and emergency levels as well as for business continuity purposes. These benefits were not realized within organizations that did not integrate the ERM function to performance measurement processes for its executives.

Benefit six: effective coordination of regulatory and compliance matters

Bond rating agencies, financial statement auditors, and regulatory examiners, have begun to inquire about, test, and use monitoring and reporting data from ERM programs. Since ERM data involves identifying and monitoring controls and mitigation efforts across the organization, this information can help reduce the effort and cost of such audits and reviews.

Through all of the benefits noted above, ERM can enable better cost management and risk visibility related to operational activities. It also enables better management of market, competitive, and economic conditions, and increases leverage and consolidation of disparate risk management functions.

38.01 Mandate

The Audit Committee shall provide oversight to the Auditor General and to the work of the City of Greater Sudbury's external auditors. The Committee shall hear presentations and receive correspondence and reports from the Auditor General *and other City staff regarding audits, the wrongdoing hotline and the City's enterprise risk management processes.*

38.02 Primary Objectives

The Audit Committee shall be responsible for the following objectives:

- (1) To review and approve the external auditor's work plan;
- (2) To review the annual Audited Financial Statements and the annual Audit Findings Report;
- (3) To review the Auditor General's reports and annual work plan
- (4) To conduct an annual review of the Auditor General's Office;
- (5) To review matters included in the Auditor General's mandate;
- (6) To study topics or issues referred to the Committee by Council resolution;
- (7) *To review and approve reports on the City's Wrongdoing Hotline; and*
- (8) *To review and approve reports on the City's Enterprise Risk Management process.*

38.03 Membership

The Audit Committee shall be composed of at least five and a maximum of seven Members of Council. An external advisor may be appointed by Committee to augment the knowledge, skills and experience of Committee members.

38.04 Term

The term of the Audit Committee shall coincide with the term of Council.

38.05 Automatic Adjournment

(1) Where a Finance and Administration Committee meeting is scheduled to begin at 6 p.m. the same day, the meeting shall automatically adjourn at 5:30 p.m. if still in session, unless otherwise decided by a two-thirds majority of the Members present.

(2) Where there is no meeting of the Finance and Administration Committee scheduled for the same day, the Audit Committee shall automatically adjourn in accordance with Articles 25.03 and 25.04.

38.05 Meeting Dates (By-law 2012-168)

Commencing in 2017, the Audit Committee shall usually meet on the same days as the Finance and Administration Committee at the end of each quarter.