

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

Presented To:	Audit Committee
Presented:	Tuesday, October 4, 2016
Report Date:	September 19, 2016
Type:	Manager’s Report

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