

City Council Memorandum

City of Arts & Innovation

TO: HONORABLE MAYOR AND CITY COUNCIL DATE: MARCH 12, 2019

FROM: INTERNAL AUDIT DIVISION WARDS: ALL

SUBJECT: DISCUSSION ON INTERNAL AUDIT DIVISION REPORTING TO CITY COUNCIL

ISSUE:

Receive and provide input on a report on the creation of an Internal Audit Division that reports to the City Council.

RECOMMENDATION:

That the City Council receive and provide input on a report on the creation of an Internal Audit Division that reports to the City Council.

COMMITTEE RECOMMENDATION:

The Governmental Affairs Committee met on February 6, 2019, with Chair Andy Melendrez, Vice Chair Mike Gardner and member Chuck Conder in attendance. Following discussion, the committee unanimously recommended that the report on creation of an Internal Audit Division to report to the City Council be forwarded to City Council for further discussion.

BACKGROUND:

On April 4, 2018, Member Conder requested a report on creation of an Internal Audit/Internal Affairs Division to report to the City Council at a future City Council Governmental Affairs Committee meeting.

LEGISLATIVE HISTORY:

City Charter, Section 701 - Organization of City operations and activities

“...The Council may, by ordinance, abolish, consolidate, modify or separate any department, office, agency, board, commission or committee, and may assign, reassign, or modify any functions, powers, or duties.

No office provided in this Charter to be filled by appointment by the City Manager may be consolidated with an office to be filled by appointment by the City Council. The City Council, subject to the provisions of this Charter, shall provide for the number, titles, qualifications, powers, duties and compensation of all officers and employees.”

2012 Charter Review Ballot Proposal (Measure E)

During the previous City Charter Review in 2012, the Charter Review Commission voted to place an amendment (Measure E) on the June 5, 2012 voter ballot. Measure E sought to amend the Charter by including a new Charter officer, the City Auditor, appointed by the City Council (with the powers and duties of the City Auditor set by ordinance of the City Council).

The final official results of the June 5, 2012 Presidential Primary Election showed a majority of residents voted against the measure (16,399 or 54%), versus those that voted in support of the measure (13,947 or 46%).

DISCUSSION:

Creation of a new Internal Audit/Internal Affairs Division

The City Council may elect to use their authority under Section 701 of the City Charter, to establish, by ordinance, a new Internal Audit office to be filled by City Council-appointed employees, who report directly to the City Council.

Current status of the Internal Audit Division

A survey conducted in December 2018 of the twelve largest cities in California noted the placement of the audit functions within each organization (see survey results below).

Survey of Audit Functions in the 12 Largest Cities in California

City	Reports to
Riverside	City Manager / Governmental Affairs Committee
Santa Ana	N/A
Anaheim	City Manager
Bakersfield	N/A
Oakland	Elected
Sacramento	Audit Committee
Long Beach	Elected
Fresno	Finance Department
San Francisco	Controller
San Jose	City Council
San Diego	Audit Committee
Los Angeles	Controller

Source: Internal Audit Division. Data obtained from surveyed City websites.

Auditing Standards Independence and Reporting Recommendations

According to standards promulgated by the Institute of Internal Auditors (IIA), internal auditors must be independent to perform their work without threats to their objectivity or integrity. Threats to independence and objectivity must be managed at the auditor, engagement, functional, and organizational levels. Proper placement of the internal audit activity within an organization can help audit shops achieve independence requirements.

The City of Riverside Internal Audit Division follows auditing standards set forth by the Government Accountability Office (GAO). The GAO's generally accepted government auditing standards (GAGAS, issued July 2018) cite reporting recommendations for audit shops that are internal to an organization. Chapter 3 (Ethics, Independence, and Professional Judgment), Section 3.56 of GAGAS notes the following guidelines for government internal auditors:

*“Government internal auditors who work under the direction of the audited entity’s management are considered **structurally independent for the purposes of reporting internally**, if the head of the audit organization meets all of the following criteria:*

- a. is accountable to the head or deputy head of the government entity or to those charged with governance;*
- b. reports the engagement results both to the head or deputy head of the government entity and to those charged with governance;*
- c. is located organizationally outside the staff or line management function of the unit under audit;*
- d. has access to those charged with governance; and*
- e. is sufficiently removed from pressures to conduct engagements and report findings, opinions, and conclusions objectively without fear of reprisal.*

Internal Audit 2015 Peer Review

In October 2015, the City Manager’s Office selected Courtney Ruby Consulting Services (CRCS) to conduct an independent audit, or peer review, of the internal audit function. The scope of work included an assessment of the following elements:

1. The internal audit function against the Institute of Internal Auditor’s guidance “The Role of Auditing in Public Sector Governance”, to determine if the function includes all of the key elements of an effective public sector auditing organization;
2. The function’s compliance with the International Standards for the Professional Practice of Internal Auditing (IIA Standards);
3. The function’s auditing practices against industry standards and best practices;
4. The function’s Fraud Hotline practices against industry standards and best practices;
5. The adequacy of the function’s performance measures; and
6. The staffing capacity of the Internal Audit Division.

As a result of the review, the Internal Audit Division undertook several recommended process improvement initiatives, including the following:

1. Formalized the role of Internal Audit through a formal charter, subsequently approved by City Council resolution on April 12, 2016;
2. Established a functional reporting relationship with the City Council through the Governmental Affairs Committee;
3. Implementing a strategy to adopt and follow generally accepted government auditing standards;
4. Established a process to ensure auditor independence and objectivity; and
5. Implementing a strategy to develop and implement a quality assurance and improvement program.

Current Internal Audit Organizational Structure

Internal Audit is an independent and objective assurance and consulting activity that is guided by a philosophy of adding value to improve the operations of the City of Riverside. It assists City Government in accomplishing its objectives through a systematic and disciplined evaluation of and improvements to the effectiveness of the organization's governance, risk management and internal controls.

To better reflect division responsibilities and to reestablish its core value-added mission and services, the Office of Organizational Performance and Audit has changed the name of the Division back to Internal Audit.

Staffing

The Internal Audit Division includes 3 full time equivalent (FTE) positions with the following budget:

	FY 2018/19	FY2019/20
Personnel	\$577,985	\$625,290
Non-Personnel	13,961	13,658
Total	\$591,946	\$641,948

Current staffing consists of one Senior Internal Auditor. The auditor is credentialed as a Certified Government Auditing Professional® (CGAP®), a certification from the IIA. As the IIA notes, public sector auditors may deal with unique needs from budget constraints to political and public pressures; the CGAP program is designed especially for auditors working in the public sector, aiding them in closing any government audit knowledge gaps while enhancing their skills and knowledge in the public sector field. Additionally, the Senior Internal Auditor is bound to the IIA's Code of Ethics, the purpose of which is to promote an ethical culture in the profession of internal auditing.

Reporting Structure

Following the peer review in October 2015, the Internal Audit Division implemented a functional reporting relationship with the Governmental Affairs Committee, to ensure the division has consistent and direct access to the City Council, as recommended in the review and required by government auditing standards.

The Internal Audit Division reports *administratively* to the City Manager or his/her designee; administrative reporting typically includes:

1. Budgeting and Management accounting;
2. Human Resource administration (including personnel evaluations and compensation); and
3. Internal communication and information flows.

The division further reports *functionally* to the City Council through the Governmental Affairs Committee. Functional oversight typically includes:

1. Approval of the Internal Audit Governing rules and any subsequent updates;
2. Approval of the Internal Audit Workplan;
3. Receiving communications from Internal Audit on the performance relative to its workplan and other matters; and
4. Making appropriate inquiries of management and Internal Audit to determine whether there are inappropriate scope or resource limitations.

This reporting structure meets the required criteria of an internal audit function working under the direction of management, as prescribed by government auditing standards. Further, it is consistent with recommendations set forth by the IIA – specifically, the International Professional Practices Framework (IPPF) Practice Advisory 1110-1 states:

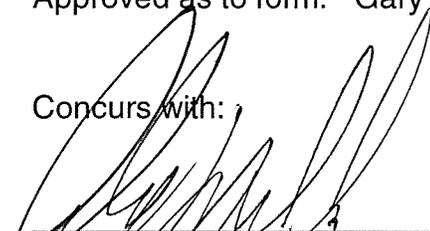
“The chief audit executive (CAE), reporting functionally to the board and administratively to the organization’s chief executive officer, facilitates organizational independence.”

FISCAL IMPACT:

There is no fiscal impact associated with this report.

Prepared by: Vincent Price, Senior Internal Auditor
Approved by: Carlie Myers, Deputy City Manager
Certified as to
availability of funds: Edward Enriquez, Chief Financial Officer/City Treasurer
Approved as to form: Gary G. Geuss, City Attorney

Concurs with:



Andy Melendrez, Chair
Governmental Affairs Committee

Attachments:

1. IIA Code of Ethics
2. Association of Local Government Auditors (ALGA) Support Letter
3. Presentation