

**CITY OF CHARLOTTE  
CITY MANAGER’S OFFICE – INTERNAL AUDIT DIVISION**

**MEMORANDUM**

To: Budget & Evaluation  
From: Greg McDowell, City Auditor  
Re: Internal Audit – Strategic Operating Plan FY12

July 26, 2011

**Internal Audit Purpose/Goals**

Internal Auditing is an independent appraisal activity established to conduct reviews of the City’s system of internal controls. The primary objective of Internal Audit is to provide reasonable assurance that the City has an operating and effective system of internal controls. A secondary objective of Internal Audit is to assist members of management in evaluating the efficiency and effectiveness of operations.

This document provides an explanation of our strategy for FY12.

|           | FY2010    | FY2011    | FY2012       |
|-----------|-----------|-----------|--------------|
| Budget    | \$905,847 | \$903,274 | \$1,045,364* |
| Positions | 9         | 9         | 9            |

\* FY2012 differs from prior budgets which did not include transfers from CATS; FY12 uses cost allocation instead

**Introduction**

Internal Audit continues to manage to its budget, reprioritizing efforts as unplanned audits are requested. As in the past, our ability to achieve these results is due to benefits gained through a stable workforce, increased efficiencies via electronic workpapers, and effective audit management by senior audit staff members. To maintain flexibility, we continued to leave a position unfilled in FY11. Instead, we chose to increase our use of audit contractors where appropriate.

Our efforts are impacted by the following:

- Unplanned Projects – The Internal Audit Division welcomes the opportunity to respond to the needs of the City Manager’s Office and KBE requests. Often, these unforeseen projects are of such importance that planned audits are delayed to accommodate them.
- Complexity – certain audits have required extensive meetings, follow-up and briefings of senior staff; e.g., County Property Tax Collections, ARRA and CATS construction.
- Follow-up – after conducting certain procurement audits, we found that some required additional reviews to ensure recommendations had been implemented.

## **Overview**

The Audit Plan includes audits in progress, regularly scheduled audits (not yet started) and additional efforts being planned, or under consideration for later years.

### Non-Competition Performance Audits:

Over the past several years, the Audit Division has increased its emphasis on non-competition audits as staff has been added and the number of competition-related audits has declined. These include: CATS construction-related audits (other direct costs, labor, overhead); Accounting and Finance operations (accounts payable, revenue collections) and city-wide activities (e.g., procurement and purchase order processing). A number of smaller audits are also conducted regularly, including Vice Imprest reimbursements, Annexation reviews (Volunteer Fire Department and Private Waste Haulers economic loss calculations), and financial capability reviews for bidders. More recently, we have conducted audits related to ARRA (quarterly reporting and individual projects), the City's ERP system development, and audits requested by the City Manager's Office (Utilities meter reading and a contract purchasing review).

It is expected that the City Manager's Office and KBEs may make special requests for audits or other support. Some time will be available for such requests as we reserve limited budget time for unplanned requests. On other occasions it may be necessary to delay a scheduled audit to address a newly identified need.

### Managed Competition Audits:

For several years, Internal Audit allocated about half its staff time to the support of the City's Managed Competition efforts. Some reductions occurred through a combination of audit efficiencies and the non-renewal of expiring competition MOUs. The audit staff time allocation decreased from 40% to about 23% between 2009 and 2011. Due to the recent suspension of the final Utilities MOU which was in place through December 2010, Internal Audit support of managed competition will be limited to SWS in FY12. Following the transition of SWS' residential model from optimization to City-wide services (for garbage, yardwaste and bulky items) along with the outsourcing of recycling in July 2010, Audit reviews the annual SWS budget and periodic results of operations. In FY11, the reviews were conducted quarterly. In FY12, we are moving to semi-annual examination of SWS results. Staff time allocated to managed completion is expected to decline substantially, requiring less than 10% of available hours.

## **Priorities for 2012**

1. Follow up Procurement Efforts – A number of procurement-related audits have been conducted in recent years, and additional follow-up is warranted. Our approach for 2012 will be to complete the Utilities follow-up and reassess where our next efforts should concentrate. That evaluation will include the following considerations:

- KBU-specific procurement follow-ups – Aviation was completed in FY08. CATS, BSS and Fire were completed in FY09, while Utilities and E&PM were completed in FY10. Two of the first six KBUs audited require limited-scope reviews to determine that recommended control improvements have been put in place. Such a follow-up for BSS was completed in early 2011, while a similar review for Utilities was nearing completion in late FY2011. The Utilities audit was expanded to include contracting processes.
  - The need for a Procurement Card audit was identified and completed in 2011. A number of actions were taken to improve controls over P-card usage.
  - Internal Audit contracted with Matrix Consulting and presented the service provider's recommendations to Council in May 2008. We focused initially on Matrix's top three recommendations: expansion of city-wide procurements under the direction of BSS/PSD; development of a city-wide construction contracting manual; and improvement of procurement-related technology capabilities. As the City undertakes the development of a new ERP system, we will review Matrix's other recommendations.
2. CATS Construction – While the South Rail Line has been operating for over three years, audits related to construction continue. In FY 2010-2011, we issued five reports focusing on light rail subcontractors. The audits have been prolonged due to the lack of vendor responsiveness to audit inquiries and requests for additional information.

Disagreements related to interpretation of Federal Acquisition Regulations (the FAR) are common. Unresponsiveness creates delays and requires additional audit work. The recommended disallowances require follow-up to determine CATS' handling of the claims. We are assessing the remaining workload related to the South Rail Line. Also, we are beginning planning efforts related to expenditures being made for the North and Northeast rail line studies. Direct labor, overhead and fees have been expended for such design work since 2004.

3. Information Technology – Audit will continue to address pre-implementation issues, including the identification of control issues related to a new ERP. We will work with the OCIO, Finance and BSS to identify other issues, which could include business process, quality control, and data integrity controls.
4. Stimulus Funds (ARRA) – Quarterly reporting will extend for a few years, and Internal Audit will continue to review the processes and accuracy related to the various KBUs' reports. After completing an audit of three grants, we are assessing other grants for an audit in 2012. In addition, we may complete a specialized audit of compliance on a specific issue, such as sub-recipient reporting.
5. Payroll – We issued a payroll-related audit in FY03 and subsequently conducted two follow-ups reviews. Rather than limiting our audit to following up past issues, we will conduct a risk analysis of current payroll operations in 2012, and define our audit scope accordingly.
6. Annual Commitments and Responsiveness – Internal Audit has committed to several repetitive audits. While none alone is as significant as the Priorities outlined above, a

number of KBUs have come to rely upon our efforts. These include five to six Vice Imprest audits per year and requests for delinquent account receivable write-offs from several organizations. Bi-annually, we audit the economic loss payments to waste haulers and volunteer fire departments related to annexation. Each year, we conduct an audit of CATS' bus operations which we submit to the City's outside financial statement auditors. In addition, we are responsive to several requests for financial reviews related to vendors the City might do business with (for financial capability), and an occasional investigation, e.g., regarding alleged theft or impropriety. Internal Audit considers it a priority to respond to each such request in a timely manner.

7. Other – While specific tasks have not been identified, it is a priority for Internal Audit to determine other areas that audits can assist the organization. For example, we have had preliminary discussions regarding support Audit could offer to those responsible for administering Federal aid/grants related to the September 2012 DNC. Separately, we have limited our audits of construction projects to those managed by CATS. Various City departments manage multiple construction projects annually. After having expanded our procurement-related audits to include the contracting process, an additional step may be to focus on the resulting construction.

### **Resource Allocation Summary**

We are staffed at 6-3/4 FTE, with one part-time temporary adding ½ FTE. Two positions are open, although the part-time temporary is funded by most of one open position. We have used remaining funds to supplement our contractor resources. Our use of contractors has been fairly steady for the past few years. We have used contracted staff at a rate of 2 to 2-1/2 FTE for the past several years.

Each staff member is required to obtain Continuing Professional Education (CPE), averaging 40 hours CPE per person to remain in compliance with Government Auditing Standards. We are being as creative as possible in the use of training funds. From 2008 to 2010, the Manager obtained over 100 leader credit hours from the Institute of Internal Auditing (IIA) after teaching classes for the organization. Half those hours have been used for staff and half for the Manager's attendance at a conference and a seminar. The credit hours were used in place of fees that would have totaled about \$4,200. While the IIA's staffing needs are uncertain, the Manager is available to teach approximately one week yearly. Any earned credits can be used to supplement the Audit Division's training budget.

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