SUBJECT: Reporting Process for Internal Audit Reports (CM07014) (City Wide)

RECOMMENDATION:

That the Reporting Process for Internal Audit Reports attached as Appendix “A” to Report CM07014, be approved.

Ann Pekaruk
Director, Audit Services
City Manager's Office

EXECUTIVE SUMMARY:

The current reporting and distribution process for Internal Audit reports (summarized in Appendix “A” of Report CM07014) provides for the distribution of the draft audit reports to management for action plans. Management's responses to the recommendations are contained in the final audit reports. This format is considered a best practice and provides valuable and timely information to members of the Audit and Administration Committee in their oversight role over the control environment.

BACKGROUND:

At the Audit and Administration Committee meeting of February 7, 2007, the Committee asked for clarification regarding the reporting process of the Internal Auditor. Staff were directed to review the current reporting process and report back to Committee with various options and/or alternatives.
ANALYSIS/RATIONALE:

At the January 5, 2005 Strategic Planning and Budgets Committee (acting in its capacity as the Audit Committee) and the subsequent January 12, 2005 Council meeting, the reporting process for Internal Audit reports was approved. This process has been updated and is detailed in Appendix “A” to Report CM07014.

As indicated in the Internal Audit Mandate, the City’s Internal Audit division is guided by the International Standards for the Professional Practice of Internal Auditing of the Institute of Internal Auditors. Standard 2440 and the related Practice Advisory 2440-1, Recipients of Engagement Results, states “Internal Auditors should discuss conclusions and recommendations with appropriate levels of management before issuing final engagement communications.” Examples of how this can be accomplished include: a post-engagement meeting (i.e. closing meeting) in which the results are discussed with management and staff of the audited area; or a review by management of the draft report with observations and recommendations by management for the audited activity. This helps to ensure that there have been no misunderstandings or misinterpretations of fact by providing the opportunity for the auditee to clarify specific items and to express views on the conclusions and recommendations.

The City’s external auditors, Grant Thornton, have also stated that discussion of recommendations with management and the inclusion of comments is important in communicating the results of audits. Grant Thornton follows this process with their Management Letters to Committee and Council and have indicated, in the past, that this should similarly be practiced by Internal Audit.

Comparisons of the current City of Hamilton process for the distribution of audit reports against the practices of other government audit groups was conducted.

City of Toronto – The draft report is transmitted to the City Manager, division head or other management representatives. Few changes (mainly format changes) are made to the draft report before the final report is prepared for distribution to the Audit Committee and City Council. Written responses are typically received from the appropriate management representative of the audited entity and submitted to the Audit Committee.

City of Winnipeg – An informal confidential draft report is forwarded to management for review and input. This input is incorporated into the report, creating a formal draft report which is again forwarded to management, now for responses to the recommendations. The responses are included in the formal draft which is presented to the Audit Committee. The report does not become a public document until the final report goes to Council.

Auditor General of Canada – The audit team drafts a document which will eventually be included in the Auditor General’s Report to the House of Commons. The audit team reviews the facts and results of audit tests with the department or agency being audited. These organizations are given an opportunity to correct facts and provide comments. The Auditor General’s Office publishes responses to each recommendation from the organization being audited. These responses are summarized at the beginning of the Auditor General’s report.
ANALYSIS/RATIONALE: (Continued)

In the United States for government internal audit groups operating under the *Government Auditing Standards*, audit reports are required to include pertinent views of the officials of the audited organization concerning the auditor’s issues and recommendations and their planned corrective action. Written responses are typically received from the appropriate management representative of the audited entity and submitted to the Audit Committee. Even though there is no statutory requirement for Canadian internal auditors in government to follow such a standard, it is considered a best practice.

ALTERNATIVES FOR CONSIDERATION:

1. The process described in Appendix “A” of Report CM07014 is recommended. It compares to the methods used by other government audit groups, provides timely and comprehensive information to the Audit and Administration Committee and Council and allows for staff to be properly prepared to answer Councillors’ questions.

2. An alternative method whereby audit issues and recommendations will be discussed with management and staff of the audited entity in a closing meeting but the actual audit report will go only to Committee without the Management Action Plans. Committee and Council will then direct management to formulate responses and bring back a separate report to a subsequent Committee meeting. This is not recommended as the delay in responding to the recommendations to a later date diminishes the impact of the audit report and the need for timely information regarding implementation plans. It also differs from practices of several comparators in that management’s responses are not included in the auditor’s report.

3. Another alternative would see no discussion of audit results with management and staff of the audited entity. The audit report would go directly to the Audit and Administration Committee and Council. Direction would be given for management to then subsequently respond to the report. This is not recommended as there would be no opportunity for auditees to ensure that there were no misinterpretations or misunderstandings in the detail before the document was made public. This option also contravenes the prescribed standard used for the practice of internal auditing which states that results and recommendations should be discussed with appropriate staff before issuing final reports.

FINANCIAL/STAFFING/LEGAL IMPLICATIONS:

Financial
None.

Staffing
None.

Legal
None.
POLICIES AFFECTING PROPOSAL:

None.

RELEVANT CONSULTATION:

The reporting process for the City of Toronto, City of Winnipeg and the Auditor General of Canada were used for comparison purposes under the Analysis/Rationale section.

CITY STRATEGIC COMMITMENT:

By evaluating the “Triple Bottom Line”, (community, environment, economic implications) we can make choices that create value across all three bottom lines, moving us closer to our vision for a sustainable community, and Provincial interests.

Community Well-Being is enhanced. ☐ Yes ☑ No

Environmental Well-Being is enhanced. ☐ Yes ☑ No

Economic Well-Being is enhanced. ☑ Yes ☐ No

City Council’s strategic commitment to “Best Practices – Best Value” under “A City That Spends Wisely and Invests Strategically” is addressed through audits and reviews whose results and management action plans for implementation are reported to Council through the Audit and Administration Committee.

Does the option you are recommending create value across all three bottom lines? ☑ Yes ☐ No

Do the options you are recommending make Hamilton a City of choice for high performance public servants? ☑ Yes ☐ No

ap:dt
Attachment
APPENDIX “A”
REPORTING PROCESS FOR INTERNAL AUDIT REPORTS

**Regular Reports**
1. At the conclusion of the fieldwork required for an audit/review, a formal audit report will be drafted. In most cases, the report will follow a three-column format – Observation, Recommendation and Management Action Plan. The first two columns will be filled in by Internal Audit. This draft report will then be distributed to management responsible for formulating a response to each recommendation. A two-week turnaround time will be allowed.

2. The responses received from management will be incorporated into the third column of the report. Responses will include an “Agree/Disagree” along with a brief implementation plan and expected implementation date or a reason for the disagreement, as warranted.

3. This report will then be circulated to the General Manager(s) of the responsible department(s) for review and approval of the Management Action Plans only. A one-week turnaround time will be allowed.

4. Upon the approval, the final audit report will be presented to the Audit and Administration Committee for receipt, discussion and staff direction.

**Follow Up Reports**
1. As prior audits are followed up, a fourth column will be added to the original audit report of a particular area/function/activity. This column will indicate the result of Internal Audit’s follow up review.

2. This draft report will be sent to appropriate staff and the General Manager(s) of the department(s) responsible for the implementation of the recommendations for information and to ensure the remarks of the Auditor are reflective of current conditions.

3. The follow up report will be presented to the Audit and Administration Committee for receipt.

**Note**
Copies of all audit and follow up reports are provided to Corporate Management Team (CMT) members for information only at the time the Clerk’s Office is requested to place the reports on the Audit and Administration Committee agenda.