



HONKAMP KRUEGER & CO, P.C.

*CPAs & Business Consultants*

## **Quality Assessment Report**

For

***Louisville Jefferson County***

***Metro Government***

***Office of Internal Audit***

*December 2, 2014*

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# Executive Summary

## Introduction

Internal auditing is one of the cornerstones of corporate governance, along with the board of directors, senior management, and external audit. Because of its unique position within organizations, internal auditing provides audit committee members and senior management with valuable assistance by giving objective assurance on governance, risk management, and control processes. To do this effectively, an internal audit function must be adequately resourced, professionally staffed, and follow the International Professional Practices Framework (IPPF). The IPPF is the conceptual framework developed by The Institute of Internal Auditors (“IIA”), the global authority, recognized leader, principal advocate and primary trainer for the profession of internal auditing. The IPPF is a comprehensive set of mandatory guidance which is principles-based and is considered the essential requirement for establishing and performing internal auditing.

The IPPF and its components are important to those who rely on and use the services of the internal audit profession. The components include mandatory guidance: the Definition of Internal Auditing, the Code of Ethics, the *Standards*, as well as strongly recommended guidance: Position Papers, Practice Advisories, and Practice Guides.

As prescribed in the Definition of Internal Auditing, an effective internal audit function acts as an independent, objective assurance and consulting activity that is designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, controls and governance processes.

A few of the benefits realized by having an established and professional internal audit department that is in compliance with The IIA’s IPPF are:

- **Identification and assessment of risks:** Internal audit helps companies identify the risks and barriers they might face in the path to achieving their business objectives. Internal audit also assesses the likelihood of the risk materializing and its possible consequences, thereby giving a perspective of what risks are “key” and therefore require more urgent management attention. Internal audit can help companies be better prepared to prevent certain adverse events from occurring and also to provide an adequate response should such events occur. This means that an organization is likely to face fewer surprises or crisis situations and be better prepared for most eventualities.
- **Evaluation and validation of controls:** Companies can assess whether the controls and procedures they have put in place are adequate to mitigate the identified risks. This enables companies to improve control procedures and make course corrections when needed. Evaluation of controls by experts in this field can help remedy gaps in internal controls and may even lead to prevention and/or detection of fraudulent risks.

- **Validation of compliance with regulations and internal policy and procedures:** Compliance with regulations as well as internal policies and procedures is a key result of the involvement of internal audit. A constant focus on this area through the internal audit function can help management promote a culture of “compliance consciousness” where compliance occurs as part of everyone’s daily work rather than as a separate process.
- **Improvement in the effectiveness and efficiency of processes:** When management extends the internal audit scope to include evaluation of enterprise risks, internal audit may identify duplicate and redundant activities.
- **Provide comfort to the Board, management and other stakeholders:** One of the most important benefits of internal audit is to provide assurance to management and a level of comfort to the Audit Committee, Board of Directors and external stakeholders that the company has a strong control environment that sufficiently mitigates the risks to which a company might be exposed and contribute towards meeting business objectives.

The IPPF requires internal auditors to develop and maintain a Quality Assessment and Improvement Program (QA&IP). In addition to both ongoing and periodic internal assessments, the QA&IP also requires an external quality assessment of the function’s adherence to the IPPF. Specifically, The IIA *Standard 1312* states that all internal audit activities are required to conduct an external assessment every five years in order to provide assurance that the activity is in conformity with The IIA *Standards*, Definition of Internal Auditing and the Code of Ethics. Government Auditing Standards require a similar exercise to be performed once every three years.

## The HK Solution

The Louisville Jefferson Country Metro Government (LJCMG), Office of Internal Audit (OIA) engaged Honkamp Krueger & Co., P.C. (HK) to conduct a Quality Assessment (QA), the fourth QA for the function. The engagement was designed to provide assurance that the activity is in conformity with The IIA *Standards*, Government Auditing Standards, the Definition of Internal Auditing and the Code of Ethics. In addition, the scope of the engagement was also designed with the objectives of providing LJCMG with any observations that would add value to the organization, its Council, and Executive Management, including identifying opportunities for improving the efficiency and effectiveness of the internal audit activity, as well as ensuring the expectations of the Council and Executive Management are being met. HK utilized proven methodology to execute this QA including:

- **Advance Preparation Form** was completed by OIA including a questionnaire by the Chief Audit Executive (CAE), as well as gathered other pertinent data which provided HK detailed information about the organization and the internal audit function.
- **Surveys** were sent to a sample of LJCMG’s management team as well as all OIA staff members, with the completed surveys returned directly to HK. The HK team compared the survey results to historical national data available. A summary of the results and accompanying comments (without identifying the individual survey respondents) has been furnished to the CAE.
- **OIA Work papers and Reports** were made readily available from which we selected a sample of completed audits from the prior 12 months.

- **Interviews** were conducted with a select sample of OIA staff as well as the following senior executives and the Chair of the Government Accountability and Ethics Committee:

<u>Name</u>	<u>Title</u>
Tina Ward Pugh	Government Accountability and Ethics Committee Chair
Greg Fischer	Mayor
Ellen Hesen	Chief of Staff
Steve Rowland	Chief Financial Officer
Sherri Toohey-Taylor	Director of Human Resources
Jason Ballard	Director of Information Technology
Glenn Wathen	Chief Information Security Officer

- **Assessment tools** were completed on the following topics:
  - Organization of Internal Audit
  - Risk Assessment and Engagement Planning
  - Staff Professional Proficiency
  - Information Technology
  - Production and Value Added
  - Crosswalk IIA *Standards* to Government Auditing Standards

## Positive Comments

OIA is seen as one the key cornerstones of LJCMG’s corporate governance, as evidenced by interviews, surveys, document reviews, and observations. We found numerous positive aspects about the OIA and the work it performs. Some of the more notable positive aspects and practices include:

- CAE included in bimonthly Mayor’s chief and director meetings
- Overall opinion in report presented using a heat map approach
- Maintains an OIA website
- Monthly Intranet Internal Control Points
- Direct feedback to OIA from the Ethics Tip Line
- Annual Risk Assessment process is based on COSO model and is well documented
- Utilizes outsourcing to gain subject matter expertise for IT auditing

## Conformity Rating

The IIA QA framework provides a system for rating conformity to the *International Standards for the Professional Practice of Internal Auditing (Standards)*, which consists of three categories: generally conforms, partially conforms, and does not conform. The framework describes these categories as follows:

- “Generally Conforms” (GC) means that an internal audit activity has a charter, policies, and processes that are judged to be in accordance with the *Standards* in all material respects, but some opportunities for improvement may exist.
- “Partially Conforms” (PC) means that practices were noted that are judged to deviate from the *Standards*, but they did not preclude the internal audit activity from performing its responsibilities in an acceptable manner.
- “Does Not Conform” (DNC) means that deficiencies in practices were judged to be so significant as to seriously impair or preclude the internal audit activity from performing adequately in all or in significant areas of its responsibilities.

The IIA *Standards* are divided into two primary subsets: Attribute and Performance. The QA team rates LJCMG’s OIA as follows:

Attribute <i>Standards</i> :	Generally Conforms
Performance <i>Standards</i> :	Generally Conforms
Code of Ethics:	Generally Conforms
<b>Overall Evaluation:</b>	<b>Generally Conforms</b>

The QA team also determined that the OIA conforms to the requirements spelled out in the Government Auditing Standards (see Addendum at the end of this report for further detail).

LJCMG’s OIA has demonstrated a commitment to quality, successful leadership practices, and maintaining an internal auditor’s mindset for professionalism. Our assessment has noted LJCMG’s OIA has developed and implemented an internal audit methodology, a set of policy & procedures, and built a team of experienced auditors based upon the principles promulgated by The IIA. This assessment further provides evidence to the board, management, and other key stakeholders that the internal audit activity adds value through improving the organization’s operations, contributing to the attainment of objectives, and ensuring a strong internal controls structure.

## Opportunities and Practice Improvement Suggestions - Summary

HK has categorized observations and recommendations into the following three categories:

- **Opportunities to Improve Conformity with IIA Standards** are deviations from the *Standards*, either by the manner in which internal audit conducts its activities and / or policy and procedures in place to guide the function. The observation of the deviation does not preclude the individual *Standard* nor the related primary subsets from “Generally Conforming”, and must be taken into consideration with the entirety of the *Standard* and the spirit and intent by internal audit to comply.
- **Practice Improvement Suggestions for Internal Audit Consideration** are observations not mandated by the *Standards* but are recommended by IIA practice advisories, IIA practice guides, team experience, or other authoritative literature.
- **Practice Improvement Suggestions for Metro Council and Senior Management Consideration** are observations outside the scope of the assessment but are recommended by IIA practice advisories, IIA practice guides, team experience, or other authoritative literature.

The opportunities and practice improvement suggestions that we believe will enhance conformity with the *Standards* and further improve the effectiveness of Internal Audit are summarized as follows.

### Opportunities to Improve Conformity with IIA Standards

1. **Expand QA&IP** to include periodic assessments of all aspects of the internal audit activity against the *Standards*.
2. **Inform senior management and the Metro Council** which auditable units cannot be addressed in a reasonable timeframe due to resource and skill limitations.
3. **Include fraud risk considerations** in the planning documentation on all engagements.
4. **Document rationale** for assignment of audit resources to an engagement.
5. **Improve documentation of engagement supervision** to demonstrate approval of planning and audit progress.
6. **Implement procedures** to improve the timeliness of audit reports.

## Practice Improvement Suggestions for Internal Audit Consideration

1. **Consider requiring due dates to reported issues** in order to facilitate the follow-up process.
2. **Consider inclusion of appropriate audit performance metrics** in LouieStat program and periodic reporting of results to the Mayor and Metro Council.
3. **Continue efforts to develop an electronic work paper system** using Microsoft Office Suite.

## Practice Improvement Suggestions for Metro Council and Senior Management Consideration

1. **Strengthen the Louisville Jefferson County Metro Government’s governance structure** by establishing a separate advisory committee to handle the functional reporting roles and responsibilities of a more independent audit committee such as:
  - Approval for the selection and removal of the CAE
  - Approval of the annual audit engagement plan or significant subsequent changes
  - Approval of financial and resource budget or significant subsequent changes
  - Approval of the CAE compensation and performance evaluation

Additional detail about the previously listed opportunities and innovative practices is provided in the Report Detail section that follows this Executive Summary. Thank you again for the opportunity to provide you with our quality assessment services.

Respectfully,



Carl A. Balderson  
Team Leader – Quality Assessment Services

David M. Walsh III  
Team Member – Quality Assessment Services

## Report Detail

### Opportunities to Improve Conformity with IIA Standards

Observation	Recommendation	OIA Response
<p><b>1. Periodic Assessments</b></p> <p>➤ <i>Standard 1311 (Internal Assessments)</i> Internal assessments must include:</p> <ul style="list-style-type: none"> <li>• Ongoing monitoring of the performance of the internal audit activity; and</li> <li>• Periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices.</li> </ul> <p>The OIA has continued to refine their QA&amp;IP over the course of the last two QA's, taking steps to establish a robust internal assessment process including establishing ongoing monitoring of the performance of OIA.</p> <p>The OIA has not also established periodic self-assessments which evaluate target areas of the group's program for evaluation. The OIA has an opportunity to further refine its periodic self-assessment by ensuring it includes all aspects of the internal audit activity, to ensure compliance with all <i>Standards</i>.</p>	<p>The OIA should enhance its current QA&amp;IP by developing periodic self-assessments to ensure all aspects of the internal audit function are evaluated in a timely manner. This includes ensuring that every <i>Standard</i> has been addressed and is being conformed to by the function. Innovative practices often utilize a rotation program with targeted annual assessment activities to ensure comprehensive coverage of the department and the <i>Standards</i> within a five year timeframe to meet the spirit and intent of the periodic assessment criteria.</p>	<p>The Office of Internal Audit will develop a self-assessment to ensure all aspects of the internal audit function are in conformance with our professional standards. The self-assessment will be performed on a periodic basis and the results will be presented to the Mayor and Metro Council on an annual basis. The self-assessment will be developed using tools noted in the Institute of Internal Audit's Quality Assessment Manual. The objective of the tools is to streamline the process for gathering evidence and performing a quality assessment on internal audit governance, staff, management and the audit process. This self-assessment will be developed by the end of the calendar year 2015 with implementation beginning in calendar year 2016.</p>

## Opportunities to Improve Conformity with IIA Standards

Observation	Recommendation	OIA Response
<p><b>2. Auditable Risks Not Being Addressed</b></p> <p>➤ <i>Standard 2020 (Communication and Approval)</i> The CAE must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The CAE must also communicate the impact of resource limitations.</p> <p>For most internal audit functions there are typically too many auditable risks within the audit universe to be able to provide complete coverage in a reasonable timeframe. Internal auditors therefore utilize a risk-based audit plan to ensure resources are focused on the significant risks to the organization. While this approach is appropriate, the CAE is still required by the <i>Standards</i> to communicate to the Metro Council and senior management what auditable risks of the organization are not being addressed timely due to resource and/or skill limitations.</p>	<p>The CAE should devise a methodology to communicate the auditable risks that are not being addressed in a reasonable timeframe, including defining what would constitute "reasonable". Typically, the communication would coincide with the delivery of the annual audit plan and discussion of resource requirements for the function. We would recommend that this communication occur at a minimum on an annual basis.</p>	<p>The Office of Internal Audit will begin to communicate the long term audit plan in addition to the one year audit plan that is reported on an annual basis. The long range plan will show stakeholders the auditable risks that are not being addressed in the near future. Communicating the long range plan will also illustrate the number of years it will take (<i>with current resources</i>) to cycle through all the high risk areas identified in our enterprise wide risk assessment. The Office of Internal Audit will begin including this information in the 2014 Annual Report of Activities and the fiscal year 2016 budget preparation documentation.</p>

## Opportunities to Improve Conformity with IIA Standards

Observation	Recommendation	OIA Response
<p><b>3. Document Consideration of Fraud Risk</b></p> <p>➤ <i>Standard 2210.A2 (Engagement Objectives)</i> Internal auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.</p> <p>Fraud can be very detrimental to any organization, and therefore should be considered a critical element within any engagement planning process. Lack of consideration of the potential for fraud may result in significant risk(s) not included as part of the engagement risk assessment process.</p> <p>Review of OIA work papers noted fraud risks were not being identified through the engagement level risk assessment process. An opportunity exists for OIA to more formally address the consideration of fraud risks and the subsequent impact the risk has on the scope of the engagement. A formalized approach ensures fraud is considered on every engagement.</p>	<p>OIA should develop a formal policy within the OIA manual requiring auditors to document their evaluation of the potential for fraud within the engagement planning process. The method for capturing the consideration of fraud within the planning process can take many forms and should be developed in accordance with a method most advantageous to OIA. In our experience it is typically evidenced by developing formal steps as part of the planning checklist or engagement level risk assessment.</p>	<p>The Office of Internal Audit will begin to require auditors to evaluate and document the potential for fraud with each audit engagement. This will be done as part of the engagement planning process and will be included as part of the audit engagement risk assessment checklist included in the background of our audit work papers. The consideration for fraud is also discussed at the planning meeting for audit engagements. We will begin to require auditors to document this discussion of fraud in the planning meeting notes. The Office of Internal Audit will develop a formal policy in our Policies and Procedures Manual to reflect these actions by February 2015.</p>

## Opportunities to Improve Conformity with IIA Standards

Observation	Recommendation	OIA Response
<p><b>4. Rationale for Staff Assignments</b></p> <p>➤ <i>Standard 2230 (Engagement Resource Allocation)</i> Internal auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.</p> <p>While decisions on how best to utilize resources is inherent to the planning phase of any engagement, the OIA has an opportunity to formalize the resource allocation process by documenting the rationale for assigning auditors to an engagement. When determining the appropriateness and sufficiency of resources, OIA management should consider:</p> <ul style="list-style-type: none"> <li>• number and experience level of the auditors</li> <li>• knowledge, skills and other competencies of the auditors</li> <li>• availability of subject matter experts where additional knowledge and competencies are required</li> <li>• training needs of internal auditors as each engagement assignment serves as a basis for meeting the OIA's developmental needs</li> </ul>	<p>The CAE should establish a written policy in the OIA Manual requiring that the rationale for assigning auditors to an engagement be documented in the planning section of the work papers. This approach ensures OIA management has taken into consideration the complexity, time constraints, and availability of resources when assigning staff to an engagement.</p>	<p>The Office for Internal Audit will begin documenting the rationale for assigning auditors to a specific engagement in the engagement assignment memorandum. This memorandum notifies the auditor of their next assigned engagement and is included in the background of our audit work papers. We will begin to implement this action immediately.</p>

## Opportunities to Improve Conformity with IIA Standards

Observation	Recommendation	OIA Response
<p><b>5. Enhance engagement supervision</b></p> <p>➤ <i>Standard 2340 (Engagement Supervision)</i> Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.</p> <p>Review of work papers noted an improvement from the prior QA in 2011 in regards to evidencing supervision by management on a timely basis at certain key phases of the engagement. Opportunity still exists, however, to further improve upon evidence of supervision during both the planning phase and ongoing throughout the engagement. We were informed that supervision may be occurring informally through periodic discussions and planning sessions with supervisory employees, however, it is not being evidenced in the work papers.</p>	<p>The extent of supervision required will always depend on the proficiency and experience of the auditors performing the work and the complexity of an engagement. With this in mind, we suggest that additional documentation of on-going supervision and review of work papers is necessary to ensure compliance with <i>Standard 2340</i>.</p> <p>Specifically, OIA should evaluate its current processes for capturing evidence of supervision during both the planning phase and ongoing throughout the engagement. A more formalized process helps to ensure this key activity is occurring on each and every engagement.</p>	<p>After the previous QAR in October 2011, the Office of Internal Audit began documenting the review and preparing review notes after certain milestones throughout the audit process (e.g., at the completion of audit program or testing). We will begin to be more consistent in this approach to ensure continuous supervision is documented not only for entry level auditors but also for experienced auditor and management as well. We will begin to implement this action immediately.</p>
<p><b>6. Timely Issuance of Audit Reports</b></p> <p>➤ <i>Standard 2420 (Quality of Communications)</i> Communications must be accurate, objective, clear, concise, constructive, complete, and timely.</p> <p>In response to the 2011 QA review, OIA management has developed key milestones within the audit engagement process which are monitored for delays in report issuance. Despite these efforts, examination of the OIA Activity Report noted that OIA continues to struggle with timely issuing of reports in comparison to the milestones they self-imposed.</p>	<p>OIA should implement procedures to improve the timeliness of audit reports. Procedures should include ongoing real time monitoring of audit reports at risk of not meeting timeliness thresholds in order to take immediate and appropriate action. Other procedures to consider depending on the cause for delays could include establishment of agreements with significant clients on response to report timeliness, and including report timeliness as a key performance metric for individual auditor's performance evaluations.</p>	<p>The Office of Internal Audit understands the necessity of issuing reports in a timely manner. The value of the report results are diminished if the report is not distributed to the Mayor and Metro Council in a timely manner. Timely communications are opportune and expedient allowing management to take appropriate corrective action.</p> <p>The Office of Internal Audit has implemented procedures in the past two years to improve the timeliness of audit reports. These efforts include the development of an Engagement Time Budget document and the modification of the Audit Time document which are both included in the work papers. We will also begin to include project completion timeliness as a key performance metric for each individual auditor's performance evaluation.</p>

## Practice Improvement Suggestions for Internal Audit Consideration

Observation	Recommendation	OIA Response
<p><b>1. Due Dates on Action Plans</b></p> <p>➤ <i>Standard 2500 (Monitoring Progress)</i> The CAE must establish and maintain a system to monitor the disposition of results communicated to management.</p> <p>In evaluating OIA's activities to monitor the disposition of audit observations we noted OIA has difficulty with assessing the timeliness of management action to address the issue. The underlying cause appears to be a lack of due dates for when management actions are to have been completed. Lacking an established and agreed upon time frame for management to take action creates an environment in which OIA is placed into an undesirable position of discussing timeliness on each audit issue.</p>	<p>We recommend OIA require management to document expected completion dates for actions to address the audit issue. This will ensure transparency to both senior leadership and OIA as to when to expect action to occur, and provides a basis for issue escalation if action is not to occur timely. In addition, OIA can schedule follow-up activities that are in alignment with expected due dates.</p> <p>This approach combined with strong management and GAEC support that continued failure to implement agreed upon actions and repeat audit observations will not be tolerated can be used as an extremely effective method to assure that implementation of corrective action has taken place.</p>	<p>The Office of Internal Audit is in the process of creating a mechanism to record, retain, and monitor management corrective actions. The Corrective Action Form is being developed using SharePoint. The Corrective Action Form will require audit clients to submit a target date for completing implementation of the corrective action. The Office of Internal Audit will begin to use the Corrective Action Form in calendar year 2015.</p>

## Practice Improvement Suggestions for Internal Audit Consideration

Observation	Recommendation	OIA Response
<p><b>2. Communicate QA&amp;IP Results</b></p> <p>➤ <i>Standard</i> 1311 (Internal Assessments) Internal assessments must include:</p> <ul style="list-style-type: none"> <li>• Ongoing monitoring of the performance of the internal audit activity; and</li> <li>• Periodic self-assessments or assessments by other persons within the organization with sufficient knowledge of internal audit practices.</li> </ul> <p>➤ <i>Standard</i> 1320 (Reporting on the QA&amp;IP) The CAE must communicate the results of the QA&amp;IP to senior management and the board.</p> <p>The OIA communicates a summary of the results of their QA&amp;IP to both the Mayor and the Metro Council, which meets the requirement of <i>Standard</i> 1320. OIA has an opportunity however to further improve transparency and allow greater oversight of the function by senior management and Metro Council by communicating the detailed results of OIA performance metrics.</p>	<p>The CAE should consider expanding upon its current reporting of its QA&amp;IP to include the detailed results of the OIA performance metrics.</p> <p>In addition, once OIA has established periodic self-assessments, as noted in the Opportunities to Improve Conformity with IIA Standards Observation #1 found on page 9, the results of the periodic self-assessments needs to be communicated to senior management and Metro Council as well.</p>	<p>As noted in the response for Observation #1, the results of the periodic self-assessments will be communicated to both the mayor and Metro Council.</p> <p>On a quarterly basis, the office of Internal audit is required to report out to the Mayor our progress as it relates to our strategic goals and initiatives. The achievement of our strategic goals is measured by our performance metrics. We will also attempt to formally communicate the progress of our strategic goals to the Government Accountability and Ethics Committee.</p>
<p><b>3. Electronic Work Paper System</b></p> <p>As noted in the 2011 QA report, OIA has developed a structured electronic work paper filing system as an interim solution until they have sufficient resources to purchase and install an automated work paper system. The current solution is sufficient to maintain operations and meets their basic retention requirements.</p> <p>We believe there is room for improving the current system, without requiring additional budget resources, which could be implemented immediately until a long term automated work paper solution has been implemented.</p>	<p>OIA should evaluate the use of Microsoft Office Suite to create, organize, share and retain its working paper documentation. A significant number of internal audit functions have established an electronic work paper system utilizing basic Microsoft Office Suite functionality such as Excel spreadsheets, Word documents, HTML, PDF, hyperlinks, etc. as their long term solutions. The use of Microsoft SharePoint software owned by LJCMG can facilitate document sharing, audit tracking, and facilitating supervisory review and approval in a fashion similar to that provided in a third party developed audit management system.</p>	<p>The Office of Internal Audit currently uses the Microsoft Office Suite to create, organize, share and retain working paper documentation. We will continue to explore the capabilities of Microsoft SharePoint, specifically the use of its work flow capabilities and for long term use in retaining work paper documentation.</p>

## Practice Improvement Suggestions for Audit Committee and Senior Management Consideration

Observation	Recommendation	Metro Council or Senior Management Response
<p><b>1. Establish an advisory committee</b></p> <p>➤ <i>Standard 1110</i> (Organizational Independence) The CAE must report to a level within the organization that allows the internal audit activity to fulfill its responsibilities.</p> <p>The legislation that established the OIA, Codified Ordinance 30.30-45, states “the Office of Internal Audit shall be separate from any other agency or department of Louisville/Jefferson County Metro Government and shall report directly to the Mayor (Executive Branch) and to the Council (Legislative Branch).” Subsequent to this legislation the Council established a standing committee called the Government Accountability and Ethics Committee (GAEC) to function as an intermediary between the Council and the OIA. Under the current legislation the Council and the Mayor’s Office share certain responsibilities for oversight of the OIA. At the same time, both have direct managerial control for all of the auditable units subject to audit by the independently established OIA. In our opinion, the current situation might be perceived as a conflict of interest.</p>	<p>As recommended in the 2011 QA, we believe governance of OIA would be improved with the establishment of an advisory committee to take over the OIA functional reporting responsibilities. This committee could be comprised of appointed members from the Council, the Mayor’s Office and local outside independent Subject Matter Experts. This committee would provide safeguards against the potential perception of a lack of independence or undue influence, thus strengthening the overall governance environment with respect to the OIA.</p> <p>Once established, we would recommend the advisory committee take ownership of the functional reporting for OIA including responsibility for:</p> <ul style="list-style-type: none"> <li>• Approving the internal audit charter;</li> <li>• Approving the risk based internal audit plan;</li> <li>• Approving the OIA budget and resource plan;</li> <li>• Receiving communications from the CAE on the OIA’s performance relative to its plan and other matters;</li> <li>• Approving decisions regarding the appointment and removal of the CAE;</li> <li>• Approving the performance evaluation and remuneration of the CAE; and</li> <li>• Making appropriate inquiries of management and the CAE to determine whether there are inappropriate scopes or resource limitations.</li> </ul>	<p>The Office of Internal Audit supports the concept of an independent advisory committee to strengthen the current governance and reporting structure. The Office of Internal Audit has developed a proposal for such a committee and presented it to both senior management and members of the Metro Council. The Chief Audit Executive also coordinated a teleconference with senior management, members of Metro Council and the Lexington Fayette Urban County Government Internal Auditor to discuss the advisory committee established in their local government. Going forward the Office of Internal Audit will advocate and champion the effort for the establishment of a truly independent advisory committee to further strengthen the oversight and independence of the audit function.</p>



**ADDENDUM Conformance to Government Auditing Standards**

December 2, 2014

Mr. Ingram Quick  
Director and Chief Audit Executive  
Louisville Metro Government Office of Internal Audit  
609 West Jefferson Street  
Louisville, KY 40202

Dear Ingram:

We have reviewed the system of quality control for the Louisville Jefferson County Metro Government (LJCMG) Office of Internal Audit (OIA) in effect from December 1, 2011 through October 31, 2014. A system of quality control encompasses OIA's organizational structure and the policies adopted and procedures established to provide it with reasonable assurance of conforming with *Government Auditing Standards* and *The Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing (IIA Standards)*. The elements of quality control are described in *Government Auditing Standards* and *IIA Standards*. OIA is responsible for designing a system of quality control and complying with it to provide OIA with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and OIA's compliance therewith based on our review.

Our review was conducted in accordance with *Government Auditing Standards*, *IIA Standards*, and guidelines established by The IIA for conducting quality assessment reviews. During our review, we interviewed and surveyed LJCMG leadership and OIA personnel and obtained an understanding of the nature of the OIA audit organization, and the design of the OIA's system of quality control sufficient to assess the risks implicit in its audit function. Based on our assessments, we selected engagements and administrative files to test for conformity with professional standards and compliance with the OIA's system of quality control. Prior to concluding the review, we reassessed the adequacy of the scope of the quality assessment review procedures and met with OIA management to discuss the results of our review. We believe that the procedures we performed provide a reasonable basis for our opinion.

In performing our review, we obtained an understanding of the system of quality control for the OIA's audit organization. In addition, we tested compliance with the OIA's quality control policies and procedures to the extent we considered appropriate. These tests covered the application of the OIA's policies and procedures on selected engagements. Our review was based on selected tests; therefore, it would not necessarily detect all weaknesses in the system of quality control or all instances of noncompliance with it.

There are inherent limitations in the effectiveness of any system of quality control, and therefore noncompliance with the system of quality control may occur and not be detected. Projection of any evaluation of a system of quality control to future periods is subject to the risk that the system of quality control may become inadequate because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate.



In our opinion, the system of quality control for the audit organization of LJCMG in effect from December 1, 2011 through October 31, 2014, has been suitably designed and complied with to provide OIA with reasonable assurance of performing and reporting in conformity with *Government Auditing Standards*, *The Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing (IIA Standards)*, and *The IIA Code of Ethics* which is a part of The IIA "*Professional Practices Framework*", in all material respects. Audit organizations can receive a rating of *pass*, *pass with deficiencies*, or *fail*. OIA has received a quality assessment review rating of *pass*.

Respectfully,

A handwritten signature in cursive script that reads "Carl A. Balderson".

Carl A. Balderson  
Team Leader – Quality Assessment Services

David M. Walsh III  
Team Member – Quality Assessment Services