



**Audit Committee Workshop Report
Wednesday, August 29, 2012
City Hall – Room 326C**

Committee Members Present: Council Members Diane Hofstede (chair), Barbara Johnson, and Betsy Hodges; Minneapolis Park & Recreation Board Representative Mark Oyaas; and Citizen Members Darrell Ellsworth and Stephanie Woodruff (quorum 4).

Also Present: Paul Aasen, City Coordinator; Casey Joe Carl, City Clerk; Magdy Mossaad, Internal Auditor; and Philip J. Bach and Kreg S. Weigand, representatives of KPMB, who facilitated the workshop.

Agenda & Synopsis

1. Agenda review, framework, and discussion of workshop goals

The facilitators summarized the themes and expectations for the workshop, based on individual interviews conducted with the principal stakeholders. Broadly, those themes included:

- Structure, scope, and objectives of audit function established under the enabling ordinance;
- Oversight responsibilities of the Audit Committee, and its implications;
- Performance and administrative responsibilities of the Internal Auditor (audit function);
- Need for education and development of a culture of risk awareness in the enterprise; and
- Organizational dynamics and management interactions and expectations of audit function.

2. Minneapolis Audit Committee:

- a) **Roles and responsibilities of Minneapolis Audit Committee**
- b) **Define success for Audit Committee performance**

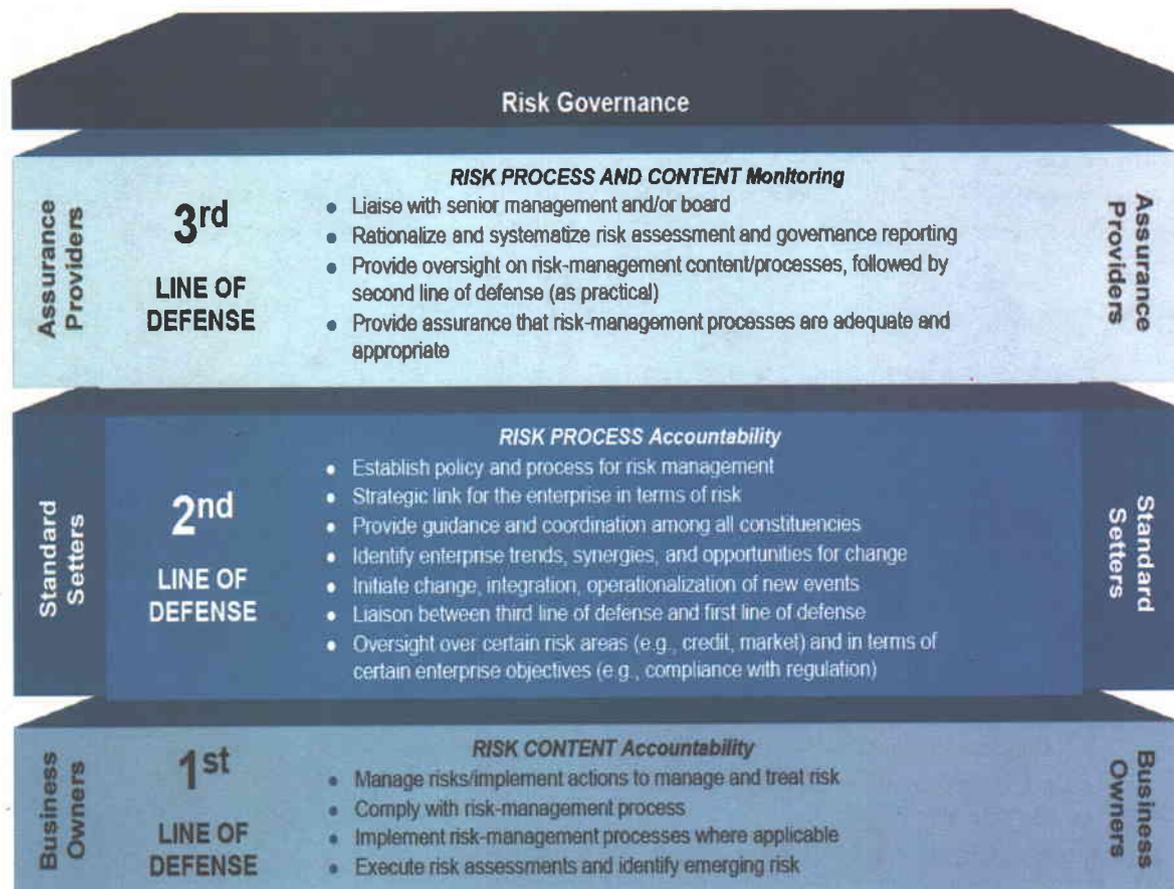
3. Internal Audit:

- a) **Roles and responsibilities of Internal Audit**
- b) **Define success for Internal Audit performance**

Under the auspices of the enabling ordinance (Minneapolis Code of Ordinances §17.90), the Audit Committee is conceived as an independent oversight body that has a unique responsibility to assure proper controls are in place to identify, mitigate, and address risk, particularly financial risk, within the enterprise. The Audit Committee does not have a role in the “governance” of the City enterprise; rather, it has a responsibility to exercise “watchful and reasonable care” in supervising the City’s internal audit function, enterprise financial reporting practices, compliance with applicable laws and policies related to financial controls, and internal controls. This last provision—internal controls—presents an inherent conflict for the Audit Committee, because it essentially expands the scope of the audit function from a singular focus on financial matters to a broader scope of evaluation by the Internal Auditor.

The leading definition of “internal controls” accepted under the audit standards promulgated by the Institute of Internal Auditors (IIA) is that internal control is “a process designed to provide reasonable assurance regarding the achievement of objectives in effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations.” Consequently, the inclusion of *internal controls* in the scope of the internal audit function (per ordinance) creates a potential conflict with regard to the perceived scope of the audit function—from the perspective of the Audit Committee and the Internal Auditor. Consequently, this was identified as a point for follow-up and possible recommendation for action by the Minneapolis City Council.

The Committee spent significant time discussing the concept of risk awareness and risk management, represented in the following graphic provided by KPMG:



Referring both to industry standards and generally accepted practices, the facilitators stated that the Audit Committee essentially has three critical functions; to-wit:

- 1) Assessing, evaluating, and monitoring the types and levels of risk facing the enterprise;
- 2) Understanding—and operating within—the “risk appetite” of the enterprise, which is defined as the level of risk deemed acceptable by the governing body of the enterprise; and
- 3) Understanding the risk management process and its impact on the enterprise.

There was interest among Committee Members to further explore the concept of risk awareness and enterprise risk management—as presented by the facilitators—and its application and relevance to the City of Minneapolis.

A further point of potential confusion is found in the ordinance (§17.80.c), which indicates that the internal audit “shall adhere to the International Standards for the Professional Practice of Internal Auditing established by the Institute of Internal Auditors” as well as other applicable industry standards. This reflection of the professional standards established by the IIA creates a clear parameter (as it is understood within the industry) within which the audit function is to operate.

A point of concern was raised with respect to the level of detail in audit findings. More specifically, in some instances audit reports identified issues or concerns, leaving management to address the resolution to such matters; in other instances, reports provided concrete guidance on the corrective course of action to be taken, leaving no little or no discretion to management. From the Committee’s perspective, instances in which guidance was provided created an operational conflict within the enterprise, since management was held accountable for performance, not the Internal Auditor. The need for separation between the audit function and management was confirmed by the facilitators. But the facilitators went on to suggest that the Internal Auditor should function as a partner to management, providing objective feedback when engaged, yet maintaining the required level of independence. Some Committee Members believe this delicate line of separation is a concern of management, resulting in some “push back” to the audit function. As a result, the Committee itself is caught in an unproductive cycle of trying to distinguish between the proper scope of the audit function and where it may, from time to time, exceed its authority and interfere with management prerogatives. This was also an issue for further discussion and consideration.

With respect to better engagement with City departments and managers, it was suggested that it may prove beneficial to the Audit Committee to engage departments in clarifying and defining the scope of individual audits that are included as part of the adopted annual audit plan. This would both help to inform all stakeholders about the scope of an audit from the outset, and also provide an educational opportunity for department heads about the value of the audit function. Mr. Mossaad indicated that he does engage departments in a pre-meeting conference to discuss audit objectives; however, he agreed that an additional step—that may include the Audit Committee—could be considered, if that was deemed helpful.

Another concern focused on whether auditing standards and practices differed between the public sector (i.e., government) and the private sector. Conflicting opinions on this issue had resulted in confusion with respect to performance expectations, roles, and responsibilities. Based on their professional knowledge and experience, the KPMG facilitators assured the Audit Committee that auditing standards and practices were the same, regardless of context; that is, the environment did not dictate the professional standards or practices which governed the audit function. However, the facilitators did acknowledge government auditing was subject to different legal requirements, such as open meeting laws, that could necessitate modified approaches to how the work was performed.

With input from KPMG facilitators on industry best practices and the evolution of audit, control, and risk functions within both public and private sector organizations, the Committee was challenged to consider whether the existing framework created by the enabling ordinance positioned the City of Minneapolis for the best possible success. It was agreed that further dialogue was needed, which would necessitate some official clarification by the City Council. Internally, the City Coordinator functions as the administrative sponsor for the audit function, as stipulated in the ordinance. Mr. Mossaad reported that his working relationship with the new City Coordinator, Paul Aasen, was positive and that he appreciated the guidance that Mr. Aasen had provided and the rapport he had established during his short tenure with the City.

4. Meeting evaluation, questions, and close

All stakeholders participated in identifying a series of “next steps” to be taken in response to the points of agreement, concern, or follow-up that had been raised during the workshop. These action items were identified as follows:

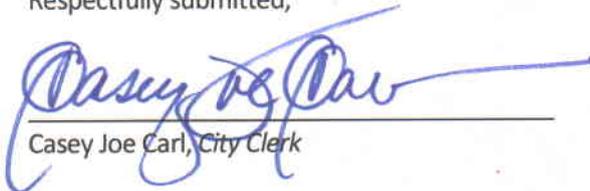
- (1) Review potential conflicts in the existing Audit Ordinance and develop recommendations for the consideration of the City Council – Chair Hofstede to take lead on this item;

[Clerk's Note: This is a strategic issue requiring additional reflection and input from the Audit Committee in terms of the recommendation(s) ultimately submitted to the City Council. The remaining items are largely of an administrative or operational nature, and will be advanced by those identified as acting in the "lead" capacity.]

- (2) Consider processes that engage department "auditees" in an earlier process to help define and scope and objectives of audits that are proposed as part of the annual Audit Plan – Chair Hofstede and Mr. Mossaad to take lead on this item;
- (3) Integrating the internal audit function more effectively into the enterprise and provide administrative sponsorship – City Coordinator Aasen to take the lead on the following series of items:
 - a. Develop plan to build enterprise risk awareness and management training, including a possible follow-up session for the Audit Committee on this topic with the KPMG facilitators;
 - b. Develop procedures to review audit reports, prior to submission, to provide input to Internal Audit related to findings and recommendations with respect to content, scope and scale of recommendations, separation of audit from management, presentation, and other factors;
 - c. Build internal awareness of the audit function and support among departments/management; and
 - d. Establish an internal escalation process whereby the City Coordinator arbitrates disputes between the Internal Auditor and management.
- (4) Conduct a periodic evaluations – Chair Hofstede and Mr. Mossaad to take the lead on these items:
 - a. Develop procedures to assure a quarterly report to the Audit Committee highlighting the progress of audits and management responses/plans; and
 - b. Determine the timing for the quality assessment reviews of the Internal Audit function, as required by the Institute of Internal Auditors.

With no further business to be presented, the workshop adjourned at 11:34 a.m. A complete copy of the PowerPoint presentation created by KPMG and referenced in the workshop is on file with the Office of City Clerk.

Respectfully submitted,



Casey Joe Carl, City Clerk