

**Program Evaluation and Audit
January 14, 2009 Presentation to the Audit Committee**

**PROPOSED RISK ASSESSMENT AND AUDIT PLAN
2009**

Requirements of the Standards

In the Institute of Internal Auditors' *Standards for the Professional Practice of Internal Auditing*, standard 2010 deals with audit planning, and requires, in part:

- That the chief audit executive (Director) establish risk-based audit plans to prioritize internal audit activities consistent with the organization's goals.
- That the audit plan should be based on an annual risk assessment created with the input of senior management and the board.

This document represents the risk assessment for 2009, as well as the proposed audit plan based on that assessment.

Risk

Risks to the Council can take many forms. Perhaps the most obvious is financial risk, where funding or the use of funding involves some risk taking. However, there are other types of risk to the Council that should be considered in an organization-wide risk assessment.

- Reputational Risk in a public organization like the Council is crucial. Harm to the Council's reputation can affect availability of discretionary funding from local, state and federal governments, and can adversely impact the Council's relationship with taxpayers in the Region.
- Similarly, program risk can affect how the Council operates. If programs are ineffective or fail to achieve their objectives, that too can have adverse effects on the Council.

This Risk Assessment attempts to consider all relevant risks to the Council and assigns audit resources accordingly.

Organization of Report

This report is organized in three parts:

- The Council's Risk Environment and general risks anticipated in 2009 and beyond,
- Specific risks affecting programs or activities of the Council,

- Proposed Audit Plan for 2009, taking into account the risks and priorities of the Council.

Methodology of Assessment

Given the breadth of the activities of the Metropolitan Council, Program Evaluation and Audit takes an inclusive approach to Risk Assessment and Audit Planning. Meetings are held with the management team of each division to discuss their perspectives on risks to the Council generally, and on risks specific to their activities. Divisional meetings were held with:

- Metro Transit,
- Central Corridor Project Office,
- Metropolitan Transportation Services,
- Environmental Services,
- Community Development,
- Regional Administration.

A draft of this assessment was also provided to the Regional Administrator's Executive Team for review and discussion prior to the presentation to the Audit Committee.

GENERAL RISK ENVIRONMENT

The Metropolitan Council focuses on a number of policy areas:

- Environmental Services works to protect the public health and the environment by providing efficient and effective water resources management,
- Metro Transit provides bus and rail transit services in the region,
- The Central Corridor Project Office is focused on the development of the Central Corridor Light Rail Line, currently in preliminary engineering,
- Metropolitan Transportation Services oversees transportation planning for the region, as well as contracted transit services opt out funding, and Metro Mobility.
- Community Development supports planning activities in communities in the region, operates a Housing and Redevelopment Authority that administers HUD programs for scattered sites across the metropolitan area, and administers grants for the regional parks system.
- Regional Administration provides centralized support for all of the business units, including service areas like Finance, Human Resources and Risk Management.

In consulting with leadership across the Council, several risks emerged that are Council-wide in nature and could affect the Council as a whole, which are summarized here to provide a picture of the Council's general risk environment.

Financial Crisis

The global financial crisis is affecting businesses, governments and individuals everywhere, including the Council, through uncertainty about interest rates, the price of goods and services and the overall effect on the population we serve.

The unemployment rate is increasing, so people are earning less and spending less. At the same time, consumer confidence declines as does the market. Businesses, small and large restructure or close altogether. The landscape is changing daily due to the impacts of the financial crisis, all of which affects government at the federal, state and local level.

New Federal Administration

At the federal level, a new President takes office in January, along with a new Congress, which will mean changes in the federal offices with which the Council regularly interacts, including Housing and Urban Development (HUD), the Federal Transit Administration (FTA) and the Environmental Protection Agency (EPA). The depth and breadth of policy changes are unknown at this time, but many that have been discussed could be broad reaching and significantly impact areas of Council functions and programs. The top priority for the incoming administration is likely to be the financial crisis.

The specifics of the President-elect's plan for the financial crisis are not yet known. However, additional infrastructure spending for transit projects could positively impact Northstar or Central Corridor or other transit projects under construction in the region.

That type of spending would also generate more jobs and income for businesses in the region that would be working on these projects.

State Government – 2009 Legislative Session

As a result of the financial downturn, state revenues have decreased dramatically creating a deficit of \$5.28 billion. Higher unemployment reduces income tax revenue, and lower consumer spending reduces sales tax revenue. Similar downturns can be seen in the motor vehicle sales tax and other dedicated taxes, like the Game and Fish fund.

Given the poor financial picture and some uncertainty due to new members in the Legislature, the 2009 session poses major risks to the Council. The risks of spending cuts or limitations are high, and some of those may affect the Council's ability to continue some services in the region.

Human Resources

Although the current labor market, given the number of people looking for work, may enable the Council to attract more applicants for open positions, there is still the concern over the significant number of retirements among key Council staff who have a tremendous amount of knowledge and experience about their area. Knowledge loss and succession planning continue to be a concern for functional areas across the Council to ensure smooth transitions and minimize the loss of skills and knowledge from retirees who are leaving. However, the larger pool of candidates may help to fill some positions that were previously left open because they were difficult to fill.

Data and Technology

Technology continues to advance rapidly, having multiple effects on operations at the Council. New automated systems and technology tools hold the promise of greater efficiency and effectiveness, but many also create areas of vulnerability that require careful planning and management. Some specific risks of new systems can include:

- Security of data and information – Systems are migrating to utilize interfaces with the worldwide web for staff and customers. The web is an effective way to collect and disburse information, but it can also expose the Council's system to viruses, worms and other forms of malicious code.
- Much Council data is public information, but some is protected as confidential, private or non-public information per the Minnesota Government Data Practices Act. More open access to data also requires providing adequate protection for non-public data collected and maintained by the Council.

- Disasters or other catastrophes can affect power supplies and other resources needed to access technology. It is important to have business continuity plans in place that ensure that resources will be available when needed.

RISKS SPECIFIC TO COUNCIL OPERATIONS

Transit

The transit systems in the metro area again posted significant gains in ridership in 2008, some of which were commonly attributed to higher gas prices. The risk that ridership would diminish in the face of cheaper gasoline did not manifest itself as ridership continued to grow throughout the end of 2008. However, there is a significant funding shortfall for 2009 that will be difficult to meet. A fare increase would have an adverse affect on the most vulnerable transit riders and could reduce ridership. Reducing service while demand is high would be counter-productive. In addition, the inability to maintain current service would likely be held against the Region by the FTA when they consider Central Corridor's application for a Full Funding Grant Agreement. Transit funding will be a high priority for the Council during this year's legislative session.

The Central Corridor Light Rail Project, currently in preliminary engineering, is the largest transportation infrastructure project in Minnesota history. Undertaking such a large project involving funding and governance from local, state and federal sources, carries with it significant risk as well. The Central Corridor Project Office has an auditor from Program Evaluation and Audit assigned there full-time to assess risks and perform audits to ensure ongoing compliance with rules, regulations and laws. However, the risks with such a large and complex project will be numerous and evolving and must be monitored throughout the duration of the project.

Finally, every three years, each Transit agency funded by the FTA goes through a Triennial Review, where a team of contracted reviewers from FTA reviews 23 areas of transit operations across the region (Metro Transit and Suburban Providers) and assesses compliance with FTA regulations and requirements. The Council's triennial review will occur during 2009.

Community Development

Contrary to previous estimates of household growth and employment, we are now looking at significantly less growth throughout the region, making us more consistent with the rest of the upper Midwest than we have been before. It is unclear what this means for the region, but it is clear that the pattern of relatively constant growth over the last few decades has changed, and that change carries some risk to the region.

Environmental Services

ES is a leader in the region and the state on water quality issues. However, change at the national level could result in new regulations for clean water, which may require costly changes at the water treatment plants managed by ES.

Additionally, changes in state regulations or major changes at the PCA or EPA could affect ES and water management in the region, which could add cost or demand infrastructure that we do not currently have.

Finally, the slowdown in housing development and construction will affect ES Service Availability Charge (SAC) collections and could affect ES budgeting and planning for system development in the region.

Regional Administration

Although the Council's workforce planning has included a significant number of retirements over the last few years and into the next several years to come, the current economic crisis may change that outlook. Employees eligible for retirement may choose to remain in the workforce as retirement investments decrease in value, or more of them may seek post-retirement employment with the Council in a different capacity through the Post-Retirement Options program. Given the level of uncertainty, workforce planning will continue to be a challenge with many changing variables.

Like many other large organizations, the Council has become increasingly dependent on information systems for its operations. Inadequate system security or poor maintenance in key internal systems like Finance, Procurement or Human Resources puts the Council at risk for compromising or losing important data. In addition, a disaster could wipe out those systems and require the Council to either have a plan for re-starting IS services or have a plan to change service delivery to accommodate the restrictions.

Program Evaluation and Audit conforms to both the standards of the Institute for Internal Auditors (IIA) and the Governmental Audit Standards (GAS). Both bodies require an external review for compliance with audit standards be completed regularly. The IIA requires the review every five years, GAS every three. Program Evaluation last had one in 2006. To conform with the more stringent government standard, we plan to conduct a self-assessment with independent validation during 2009. It will follow the same process as in 2006. Our thorough assessment, including its workpapers, will be reviewed by the independent validator, who will then interview key people around the Council, as well as at least one member of the Audit Committee before rendering an opinion as to whether we do or do not conform to the standards. The validator would be a trained, certified validator from the Twin Cities chapter of the IIA.

2009 AUDIT PLAN

Objective

This plan reflects activities where the risk assessment indicates a high priority and high risk for the Council. Approximately 70% of all auditors' time is allocated to this plan. The remaining 30% is left open to allow for consultations, client requests and investigations where needed.

This plan does not include a detailed list of projects for the Central Corridor Project Office. Due to the evolving nature of this project, audit needs are difficult to anticipate in advance and therefore, the plan is left flexible to meet project needs in this early phase. Projects generated through the ongoing risk assessment of CCLRT will be brought to the Audit Committee as they arise.

Given the risks discussed in the previous section and the established priorities of the Council, Program Evaluation and Audit proposes to audit the following topic areas during 2009.

Regional Administration (Council-wide)

Human Resources
Information Systems Governance
Accounts Payable
Employee Benefits

Transportation (Transit and Metropolitan Transportation Services)

UPA Projects
Transit Modal Allocations
Grants and subrecipient agreements
PIMs (MTPD)
MT Construction Grants

Environmental Services

I/I Grants
Uniform Contract Administration
Tiller Corporation Contract

In addition, Program Evaluation and Audit performs the following recurring audits each year, at the request of the client organization.

Assurance Projects (Recurring)

Transit Farebox Reviews (all garages within the year)
Transit Store Cash Counts (twice per year)
Transit stockroom inventories (cyclical over 3 years)
Parks Operating and Maintenance Cost Review
Environmental Services Overhead Rate Verifications

There are also some periodic reviews that we know will be coming in a particular year.
There are two for 2009.

Planned External Reviews

FTA Triennial Review (Metro Transit and MTS)
Review of Program Evaluation and Audit – Self-Assessment with Independent Validation
(through Twin Cities Chapter of Institute of Internal Auditors) – last done in 2006.