

Program Evaluation and Audit 2012 RISK ASSESSMENT AND AUDIT PLAN DRAFT – January 2012

RISK ASSESSMENT NEEDS AND REQUIREMENTS

Requirements of the Standards

The Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing* Standard 2010 on Audit Planning 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 contains the risk assessment for 2012, 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 critically important. Harm to the Council's reputation can adversely impact the Council's relationship with taxpayers in the region, as well as affect the availability of discretionary funding from local, state and federal government sources.
- Similarly, program risk can affect the effectiveness of Council operations. If programs are ineffective or fail to achieve their objectives, that too can have significant adverse effects on the Council.

The risk assessment attempts to take into account all relevant risks to the Council and assign audit resources accordingly.

Organization of the Report

The report is organized in three parts:

- The Council's risk environment and general risks anticipated in 2011 and beyond,
- Specific risks affecting programs or activities of the Council,
- Proposed audit plan for 2012, taking into account the risks and priorities of the Council.

Methodology of Assessment

Given the breadth of 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,
- Metropolitan Transportation Services,
- Environmental Services,
- Community Development,
- Regional Administration.

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

There are a number of parties involved in the project who want to direct where the contingency funds should be spent. Depending on how the decisions are made and what is chosen, some betterments for CCLRT could delay the completion of the project.

The Southwest Corridor light rail has just gotten underway. A project office is being located and staffed, and work will begin soon to solicit potential engineering firms for the project. The Southwest project will benefit by learning from any missteps made in the previous light rail projects, HLRT and CCLRT.

Community Development

The U.S. Department of Housing and Economic Development made reductions to the Section 8 program last year. Although the Council's HRA has been able to serve all of its clients, reductions to administrative funding have strained the staff's ability to manage the caseload.

The Council is receiving a federal grant for the "Corridors of Opportunity" program to promote transit-oriented development that facilitates non-automobile transportation (biking, walking, mass transit). However, much of that funding will be sub-granted to sub-recipients charged with the actual corridor development projects. Monitoring sub-recipients and enforcing federal regulations will be a significant undertaking for the Community Development Division. Yet the Council, as the primary recipient, is responsible for the federal compliance for all sub-recipients receiving funding through the Council. In their 2010 review of the Council, the Office of the State Auditor found that the Council, in its transportation programs, did not adequately monitor sub-recipients. Monitoring requirements for the HUD grants are essentially the same as those for transportation grants. To avoid negative enforcement actions by the federal government, it will be critical to establish sound monitoring practices and documentation across the Council.

Environmental Services

Environmental Services is almost always at risk for policy/regulation changes from the federal (EPA) or state (PCA) level that could affect core operations of the wastewater system.

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, light rail and commuter rail transit services in the region,
- The Central Corridor Project Office is focused on the development of the Central Corridor Light Rail Line, awaiting a full funding agreement from the Federal Transit Administration within a few months to continue its construction, and planning to begin operations in 2014. Closely related to CCPO is the other “New Starts” project in the region, the Southwest Corridor Light Rail Project, currently awaiting federal approval for preliminary engineering.
- Metropolitan Transportation Services oversees transportation planning for the region, as well as contracted transit services, funding for suburban transit providers, and Metro Mobility.
- Community Development informs the land use planning activities of local governments as prescribed in the Land Planning Act; administers grants for the regional parks system, and the Livable Communities Act; and operates a Housing and Redevelopment Authority that administers rental assistance programs in communities throughout the metropolitan area.
- 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. Those are summarized here to provide a picture of the Council’s general risk environment. Risks to specific program/policy areas of the Council will appear in the next section, “Risks to Specific Council Programs.”

Continuing Slow Economic Recovery

The United States economic outlook continues to be mixed. Economists largely agree that we will avoid a double dip recession, and inflation is being managed. However, continuing concerns about debt crises in Europe have adversely affected Wall Street and do nothing to increase consumer confidence. A slow growth rate is predicted through the first half of calendar year 2012.

Unemployment continues to a significant problem nationally, but the rate declined in the last quarter. The state fiscal year runs from July 1, 2011 through June 30, 2012. Receipts for the first quarter of the state fiscal year are slightly (.6%) higher than forecasted, but the positive variance is not statistically significant. We cannot predict what will be the receipts for future quarters on this basis.

The impasse in the federal supercommittee on the budget will result in mandatory reductions to federal programs in 2013.. Transportation Secretary Roy LaHood has commented that cuts to transportation funding will be significant.

RISKS SPECIFIC TO COUNCIL PROGRAMS

Transportation

Federal funds provide key assistance to the programs of both Metro Transit and Metropolitan Transportation Services. The status of federal funding remains unclear until the automatic budget cuts at the federal level are finalized. Meanwhile, the Central Corridor Light Rail project (CCLRT) continues to draw federal funds, and the Southwest Light Rail is in preliminary engineering, also drawing some funds from the Federal Transit Administration.

As noted above, the state's budget picture is improving based on the current forecast and MMB estimates. The current budget (passed last session) contained significant cuts to transit services. The funding shortfall for Metro Transit is exacerbated by the fact that the State Legislature never fully funded the operational costs of the Hiawatha Light Rail and has yet to provide operational funding for the Northstar Line. Maintaining good service will be a challenge for Metro Transit. If the Legislature does not restore some funding for Transit's allocations from the State's General Fund, then the impact of the budgetary crisis will be far worse and could have major impacts on transit services in the region.

Although the greatest area of concern is around reducing costs and finding a way to meet funding reductions, the Council's transportation programs also suffer from administrative overload. In the last 5 years, the Council has opened the Hiawatha Light Rail, the Northstar Commuter Rail, expanded some bus service options, and begun construction of the Central Corridor Light Rail, with yet another rail line is in preliminary engineering. Yet during that time period, administrative support staffing and funding (Human Resources, Finance, etc.) has remained the same as they were in 2005. Sometimes, these areas seem like easy cuts, but maintaining unreasonably large workloads at such a high level increases the risk of significant errors, internal control failures and potentially even fraud.

Another limitation in transit funding, regardless of the source, is usage. There are many opportunities to obtain grants and funding for capital projects. However, there are very few sources for operating funds. The Council received federal, state and local funding to build the Hiawatha Light Rail line, but it has never received full funding for operations, although that was promised by the State Legislature. The Northstar line was similarly funded by the federal government with matches from state and local units of government, but as yet has received no operating allocation.

Locally, the Council, especially in complex New Starts projects like CCLRT, maintains complex working relationships with other entities, including the University of Minnesota, the Regional Rail Authorities, Counties and Cities. The Council also works closely with Suburban Transit Providers. These relationships are multi-faceted and require a great deal of time and attention to maintain. Maintaining these relationships is critical to the Council's success in much of its transit work.

Also, the CCLRT project, as required by the federal government, has a fairly large amount of contingency funding set aside, much more than was set aside for either Hiawatha or Northstar.

RISKS TO SPECIFIC COUNCIL PROGRAMS

Transportation

Metro Transit has taken significant budget reductions but managed to avoid service cuts and fare increases, despite the cut in the state general fund monies appropriated to the Council for transit. However, the reductions were offset with one-time money(right-of-way funds) that is no longer available. If the cuts to Metro Transit remain, there may be service reductions and/or fare increases to meet budgetary levels.

The CCLRT project is still under construction. It will reach some construction milestones in 2012. At the same time, the SWLRT project is in preliminary engineering and is beginning to create a project office.

The Federal Transit Administration (FTA), which provides the funding and oversight for the Council's federal transportation funding. Under federal law, they may choose to review compliance in a number of areas at any time. In 2012, notice has already been provided that FTA will conduct three reviews at the Council.

- Triennial Review – a comprehensive review of transit programs for 24 areas of compliance. These reviews are conducted once every three years, and our last review was 2009.
- Procurement Systems Review – an audit of procurement policies and practices. A sample of individual purchases and contracts will also be evaluated.
- Disadvantaged Business Enterprise (DBE) Program – Examines how well the Council's DBE program and activities meet the requirements of federal laws and regulations.

Community Development

A Program that runs with both transportation and housing goals creates risks because it is a new program to the Council, and compliance requirements are still under development.

The "Corridors of Opportunity" program, administered by the US Department of Housing and Urban Development (HUD), funds transit-oriented development (TOD) in the region. The program will distribute funds using local non-profit organizations. The Council has had findings in two federal and one external audit from the Office of the State Auditor. Non-profit organizations, especially newer ones, often lack an accountability structure that will facilitate their compliance with and reporting of federal requirements. Diligent monitoring of subrecipients will be required.

Community Development also administers the Livable Communities Program. It is unclear what the future of Livable Communities will be, or if the Legislature will continue to fund it. These grants, too, have been largely distributed to subrecipients, most often local units of government.

Environmental Services

Environmental Services is almost always at risk for policy/regulation changes from the federal (EPA) or state (PCA) level that could affect core operations of the wastewater system.

PROPOSED 2012 AUDIT PLAN

Objective

This plan includes projects where the risk assessment demonstrated a high level of risk and priority. Approximately 70% of the auditors' time is allocated to this plan. The remaining 30% is left open for emergent risks, requests, and investigations, where needed.

Program Evaluation and Audit proposes to schedule the following reviews in 2012:

Transportation

The engineering contract and start-up activities for the Southwest Corridor Rail Line project
Construction contracts for CCLRT
DBE program compliance for CCLRT
"Auto Reload" program for Transit GoTo cards(Metro Transit)
Construction review of the Light Rail Operations and Maintenance Facility expansion
Fare compliance – HLRT, buses
JARC/New Freedom subrecipient monitoring/compliance review
Cedar Avenue Busway – subrecipient review
Interchange Project – subrecipient Review

Community Development

Corridors of Opportunity Subrecipient Monitoring
Livable Communities grants

Regional Administration (Council-wide)

FMLA administration and Management
Contract Management Policies and Practices

Environmental Services

Review of liquid waste system – volume, billing, payments
Review policy and operation of the Central Car Pool (administered by ES, but used by all areas of the Council except Metro Transit)