

# OFFICE OF THE CITY CONTROLLER



**FISCAL YEAR 2013**

**AUDIT PLAN**

**Ronald C. Green, City Controller**

**David A. Schroeder, City Auditor**



OFFICE OF THE CITY CONTROLLER  
CITY OF HOUSTON  
TEXAS

RONALD C. GREEN

September 30, 2012

The Honorable Annise D. Parker, Mayor  
City Council Members  
City of Houston, Texas

SUBJECT: Office of the City Controller  
Fiscal Year 2012 Audit Plan

Dear Mayor Parker and Council Members:

I am pleased to submit to you the Fiscal Year 2013 Audit Plan. The basis of this year's Annual Audit Plan (Audit Plan) was an Enterprise Risk Assessment (ERA) performed by the Audit Division as required by the applicable professional auditing standards (ERA report to be issued under separate cover). Additional consideration is given to input from your Office, City Council Members, and Department Directors. This document will serve as the primary work plan to carry out the audit responsibilities in an efficient and effective manner. To enhance our effectiveness, our approach is balanced by conducting the audits using, in-house staff and by outsourcing some projects requiring certain technical or specialized skills.

This Audit Plan includes performance, compliance/contract, monitoring, continuous auditing, and unannounced audits. Additionally, the plan provides for follow-up procedures and special projects.

We post the status of progress in executing our audit plan on a quarterly basis on the Audit Division webpage within the Office of the City Controller website.

Respectfully submitted,

Ronald C. Green  
City Controller

Xc: Waynette Chan, Chief of Staff, Mayor's Office  
Andy Icken, Chief Development Officer, Mayor's Office  
Department Directors



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## BACKGROUND AND AUTHORITY –

The City Controller is an independently elected official who is granted the authority (through the City Charter, Article VIII, Section 7) to “... *be responsible for conducting internal audits, in accordance with professionally recognized auditing standards, of the operations of all City departments, offices, agencies and programs. The scope of internal auditing shall encompass an objective and systematic examination of evidence to provide an independent assessment of the efficiency and effectiveness of the city's system of internal controls and the quality of performance based on quantifiable criteria in meeting objectives....*”. The City Controller assigns this responsibility to the City Auditor (through appointment) to be the executive in charge of the Audit Division, whose scope of work is contained under a separate Charter (Audit Division Charter). Audit results are issued to the Mayor, City Council Members and Department Directors.

### AUDIT DIVISION ORGANIZATION –

During FY2012, the Audit Division reduced staff by 2 FTE's bringing the total headcount to 12, consisting of 10 professional Audit Staff, one support staff, and the City Auditor. The Audit Division has two primary sections, which consist of Audit and Information Technology (IT) Audit. Each section provides audit related services as their primary objective; however the IT Audit section is focused on Data Analysis as support for determining control risk around the key information systems, as well as the overall view of Information Technology throughout the organization. As we receive additional training, certifications, and experience, we will continue to increase our ability to provide enhanced and value-added services.

The Controller's Office utilizes internal and external audit resources to execute our mission and objectives and meet the needs and requests of our varied stakeholders. Additionally, we have 9 professional service firms under contract through March 15, 2016.

### APPROACH AND METHODOLOGY –

The Audit Division adheres to: 1) the *Government Auditing Standards* (GAS – commonly referred to as the “Yellowbook”) as promulgated by the Government Accountability Office (GAO) and 2) the International Standards for the Professional Practice of Internal Auditing as issued by the Institute of Internal Auditors (IIA – known as the “Redbook”). To assure compliance with these professional standards, the Audit Division undergoes a peer review every 3 years.

The Annual Audit Plan is a *flexible* commitment of the Audit Division within the Office of the City Controller to perform engagement activity related to the responsibility and authority identified in the City Charter as quoted above. The Audit Plan, which is approved by the City Controller, serves as a working document that considers items such as; the Enterprise Risk Assessment (ERA), input from Mayor, City Council, Department Management, and results from previous audits, etc. Due to the continual requests for audit services, the increasing demand for non-audit services, and the required testing for planned activities, the Audit Plan will be monitored and revised as necessary throughout the year. To enhance communication and facilitate transparency, the City Auditor is presenting status and results to the Budget and Fiscal Affairs Committee semi-annually.

The professional standards noted previously require that the Audit Plan be rooted in risk-based methodology. Historically, the Audit Division had outsourced its risk assessment process to external consultants and utilized the results provided in a report to assist in developing the annual audit plan. The previous risk assessments had been performed in 1994, 1999, and 2004 respectively. In FY 2010, the Audit Division conducted the ERA internally and utilized approximately 3 full-time equivalents (FTEs). Since then, the ERA is being executed annually on selected Departments on a rotational basis for efficiency and to ensure full coverage of all City Departments over a 4-5 year period<sup>1</sup>.

<sup>1</sup> See 12-02 FY2011 ERA Update under separate cover.



Evaluating all of these various factors provides indicators on prioritizing the potential projects for the upcoming year. In other words, this points us in the direction of “*what*” to audit. We then identify the available resources to determine the volume of activity to include in our plan (see Audit Resource Allocation section below).

#### **AUDIT RESOURCE ALLOCATION –**

Annually, the Audit Plan prioritizes the Audit Division’s limited resources of budgeted staff and funds based on the previously referenced risk assessment. The Audit Plan, therefore prioritizes expending efforts on either common Key Business Processes or Departments having a perceived high or moderate risk profile rating. As such, the City’s audit function serves as a risk management resource through the development of improved controls and the testing of existing controls.

The number of projects that are proposed is based on consideration and an evaluation of:

- Current headcount within the Audit Division;
- Average number of hours used on a typical audit engagement<sup>2</sup>;
- Other types of ongoing services that the Controller’s Office provides; and
- Unplanned requests from Mayor, City Council, or other Department Management,

#### USE OF EXTERNAL CONSULTANTS

For projects that involve circumstances where; 1) The use of experts/specialists is required; 2.) The independence of the Audit Division as an organization is impaired; or 3.) There is the potential for significant political sensitivity, the Office of the City Controller may elect to use external consultants. NOTE: A budgeted dollar amount is approved for the use of these resources.

#### **AUDIT PROGRAMS –**

Upon the City Controller’s approval of the Audit Plan, specific audit programs will be developed for each activity to be audited within the fiscal year ending June 30, 2012. The audit programs will be designed with regard to business services, compliance and other requirements, performance considerations, management input, and specialized skills in order to meet the specific audit objectives of each project. All audit programs, workpapers, and reports will be prepared in accordance with:

- Relevant standards issued by the American Institute of Certified Public Accountants;
- Government Auditing Standards (*Yellow Book*); and
- The Institute of Internal Auditor’s International Standards for the Practice of Internal Auditing (*Red Book*).

Where applicable, disclosure of nonconformance will be provided.

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<sup>2</sup> The Audit Division is a member of the Association of Local Government Auditors (ALGA), which provides aggregated data on internal auditing for local governments, including resource utilization (average number of hours per project).



**STATUS AND UPDATES TO ANNUAL AUDIT PLAN –**

The specific projects conducted throughout the year may be a sub-set of the list provided in the Audit Plan. The nature, extent, and timing of audit activities will vary as a result of the differences in the nature of operations, organizational structure, and management style as well as by the competence, employee capabilities, and concepts of operational control.

The Audit Division will also provide any assistance to City’s management or City Council when they request special projects (*assuming the available resources exist, and depending on the context and priority of the assignment as it relates to risk, exposure, fraud, waste and/or abuse*). These special projects will normally be performed in addition to planned audit work. If the assistance requires the use of external consultants, additional funds may need to be provided by the appropriate departments and/or City Council.

Executing the Audit Plan involves an update and status process that is scheduled weekly between the City Auditor and the City Controller. Additionally, the Audit Division posts a high-level status report on the Audit Division’s website, accessible from the City Controller’s Webpage. Post-Audit Surveys are completed and Requests for Audit Services are also available from the Audit Division’s website.<sup>3</sup>

**ANTICIPATED BENEFITS OF AUDIT ACTIVITIES –**

Compliance



Improve Accountability



Cost Savings



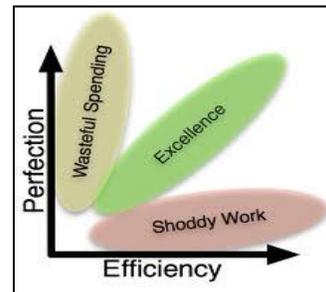
Improve Risk Management and Internal Controls



Improve Financial Reporting



Improve Efficiency



<sup>3</sup> The Audit Division has a website accessible from the Controller’s website, which post results of audits, follow-up procedures, and status of progress. SEE: <http://www.houstontx.gov/controller/audit>



## FISCAL YEAR 2013 PLANNED ACTIVITY (PROJECTS)

The following is a list of projects for the FY 2013 Annual Audit Plan. The Audit Process, while often tracked in a linear fashion, is truly dynamic and reacts to evidence, impact, and magnitude of discovery occurring during the entire engagement process. That being the case, the list provided, gives a population of projects from which to execute. The Office of the City Controller's Audit Division posts status/progress of projects on the Audit Division website and meets with the City Controller weekly and the Budget and Fiscal Affairs Committee of City Council twice a year. This provides a level of transparency and accountability for meeting our goals and objectives as set herein.

### COMPLIANCE/PERFORMANCE/FINANCIAL AUDITS AND PROCESS REVIEWS

#### ADMINISTRATION AND REGULATORY AFFAIRS DEPARTMENT (ARA); INFORMATION TECHNOLOGY DEPARTMENT (ITD)

##### COMPLIANCE AND PERFORMANCE AUDIT – P-CARDS

**DESCRIPTION:** P-Cards are used throughout the City and involve vendors/merchants, the bank that issues and processes the detail information, interface with the ERP/SAP. Because of the volume, complexity and number of entities/systems involved, the Audit will focus on reviewing current controls over the issuance, use and approval of P-Cards and the verification of the accuracy of information posted/interfaced to the ERP/SAP system.

#### FLEET MANAGEMENT DEPARTMENT (FMD) –

##### CONTRACT COMPLIANCE/PERFORMANCE – VEHICLE REPLACEMENT PART SUPPLY CONTRACT WITH NAPA

**DESCRIPTION:** Several City Departments acquire, maintain, and dispose fleet vehicles that vary from standard automobiles (fuel, hybrid, and electric), trucks (pick-up, straight, dump, etc.), heavy equipment, and specialized vehicles for specific purpose (Fire, Emergency Medical Transportation, Waste, etc.). During FY2011 Fleet Management functions from various departments was consolidated into a newly formed Fleet Management Department. The process for managing spare/replacement parts inventory was outsourced to the Genuine Parts Company (NAPA) as supported by City contract #4600010761. The total contract value was \$95 million over a 5 year term. Since the inception of the contract, the City has paid the vendor approximately \$16 Million. The audit will focus on compliance with key contract terms and management controls in place to monitor the contract activity, spending, and efficiency.

#### HOUSTON DEPARTMENT OF HEALTH AND HUMAN SERVICES (HDHHS)

##### PERFORMANCE/COMPLIANCE – PHARMACY INVENTORY

**DESCRIPTION:** Approximately \$9.1 Million was spent on Lab, Drugs, and Medical Chemical Supplies during the FY2011 while the Inventory Balance was approximately \$16.7 Million for the same period. Audit Division will review Pharmacy inventory processes, controls and record-keeping to determine if inventory is ordered, received, issued, stored, and maintained in compliance with various requirements (current Federal, State, City, and manufacturer).



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## **HOUSTON FIRE DEPARTMENT (HFD);**

### **BUSINESS PROCESS REVIEW AND COMPLIANCE – HUMAN RESOURCE MANAGEMENT**

**DESCRIPTION:** HFD has between four and five thousand active employees, which represent approximately 25% of the City workforce. Managing Human Resources of a major public safety function within the City has many considerations such as experience, training, health, adequate coverage and response, diversity, succession planning, etc. The audit will focus on the controls in place that ensure HFD workforce meet the strategic objectives of public safety.

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## **OFFICE OF BUSINESS OPPORTUNITY (OBO)**

### **MEMORANDUM OR REPORT REVIEW AND COMPLIANCE – MINORITY AND WOMAN BUSINESS ENTERPRISE (MWBE) PARTICIPATION**

**DESCRIPTION:** The City requires vendors performing contract services to provide a 'good faith effort' in utilizing MWBE as sub-contractors. The initiative is structured to encourage development of small minority/women- owned businesses. The review will look at current participation and provide an analysis of quantitative results.

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## **PUBLIC WORKS AND ENGINEERING (PWE) –**

### **PERFORMANCE AUDIT – ENGINEERING AND CONSTRUCTION**

**DESCRIPTION:** The Audit Division will review the customer utility service system, while considering the following potential objectives: (a) Accuracy of meters that support customer billing, (b) Business Processes that validate customer billing, including the protocol for working through 'service' concerns expressed by our customers (checking meters, reasonableness of billing amount, etc.) (c) Current constraints that may be in place in our ordinance(s) that could be re-framed to minimize legal pressures imposed on customers

And/or

### **PROCESS REVIEW – ACCOUNTING FOR PROP 1/SPECIAL REVENUE FUNDS**

**DESCRIPTION:** Proposition 1 was passed in November 2010, which created the need for changes to process and accounting of various activities related to infrastructure develop/re-development. The audit team will review, document and walkthrough a series of activities to identify key business processes, project set-up, tracking, and management of out-sourced functions.

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## CARRYOVER AUDITS FROM FY2011 AUDIT PLAN

The following projects began during FY2012 and are being completed in FY2013:

### **HOUSTON AIRPORT SYSTEM (HAS)–**

#### **COMPLIANCE AUDIT – OFF-SITE PARKING VENDORS**

**DESCRIPTION:** HAS has several contracts for concessions, parking management, and off-site parking. The concession contracts and the off-site parking are based primarily on self-reporting by the vendor, while the parking management is a paid contractor to handle cash for the parking facilities located at the various airport terminals. The audit team is performing a compliance audit of the self-reporting vendors for Off-site Parking and the internal controls associated with oversight to ensure revenues due to HAS/COH are identified, reported and collected.

### **HUMAN RESOURCES (HR) –**

#### **PERFORMANCE AUDIT/CONTRACT COMPLIANCE – EMPLOYEE BENEFITS**

**DESCRIPTION:** During FY2011, the City changed its employee benefits program and engaged in a contract with a new vendor to be the administrator over medical benefit activities. This marks a change from a coverage program represented by premium payments to the shift of risk to the City by paying actual medical costs for employee health care. The audit will focus on the bidding process, employee premiums, and employer payments, etc.

### **HOUSTON FIRE DEPARTMENT (HFD);**

#### **BUSINESS PROCESS REVIEW – EMERGENCY MEDICAL, CLEANING AND OFFICE SUPPLIES**

**DESCRIPTION:** HFD provides EMS, including transportation services for people in need of emergent care. At the request of HFD management, the Audit Division is identifying and documenting processes and procedures for: procurement, receiving, internal distribution, and consumption of these items.

### **INFORMATION TECHNOLOGY DEPARTMENT (ITD) – (OUTSOURCED)**

#### **CONTRACT COMPLIANCE – LOCAL TELECOM EXPENSE (LANDLINES ONLY)**

**DESCRIPTION:** The City spends approximately \$10 - 12 Million per year on local landline telephone services. The rates for services are per contract and subject to tariffs. The audit tested existence of lines being charged and the accuracy of the charges per the agreement or the appropriate tariff/rate.

### **ADMINISTRATION AND REGULATORY AFFAIRS DEPARTMENT (ARA)–**

#### **CONTRACT COMPLIANCE AUDIT – STRATEGIC PURCHASING DIVISION (SPD) CONTRACT MANAGEMENT**

**DESCRIPTION:** ARA/SPD negotiates and engages in large contracts for goods and services on behalf of the City. Some of these contracts have guarantees over pricing to ensure the City is paying the lowest possible price. The audit has examined and tested a contract for goods and/or services to verify compliance with contract terms. The report is scheduled to be released in October, 2012.



## ALTERNATIVE AUDIT PROJECTS FY2013

The Audit Plan is flexible based on changes to scope, staffing, access to information and other factors. If time and resources permit, the following projects may be substituted for or performed in addition to the previously identified projects.

### HOUSTON AIRPORT SYSTEM (HAS)–

#### COMPLIANCE AUDIT – TERMINAL PARKING

**DESCRIPTION:** HAS has several contracts for concessions, parking management, and off-site parking. The parking management is a paid contractor to handle cash for the parking facilities located at the various airport terminals. The estimated revenue for terminal parking is \$65 - \$70 million per year. The audit team will focus on vendors for terminal parking and the internal controls associated with oversight to ensure revenues due to HAS/COH are identified, reported and collected.

### HOUSTON POLICE DEPARTMENT (HPD)–

#### COMPLIANCE AUDIT – SUPPORT OPERATIONS, PROPERTY ROOM

**DESCRIPTION:** In the recent past, HPD has implemented a new Evidence Management System (EMS) and moved their property room to a new location. In addition, they have implemented Daily and Close-out audits. This audit will focus on ensuring the accuracy of the EMS and compliance with their policy and procedures.

### GENERAL SERVICES DEPARTMENT (GSD) –

#### CONTRACT COMPLIANCE AUDIT – CONSTRUCTION AND RENOVATION

**DESCRIPTION:** GSD engages in contracts in construction activity for projects and maintenance of City assets. During FY2011, GSD spent approximately \$8.5 Million on these services to outside contractors. The audit will focus on compliance with contract billing terms and change order processes.

## SPECIAL PROJECTS & ONGOING MONITORING PROCEDURES

#### A-133 SINGLE AUDIT ASSISTANCE

**DESCRIPTION:** The external audit of the Comprehensive Annual Financial Report (CAFR) has typically involved at least 2,000 hours of billable time to perform testing and preparing the report associated with grants that are subject to the A-133 compliance requirement. Due to the American Recovery and Reinvestment Act (ARRA), the required amount of testing has substantially increased. During FY2012, the Audit Division tested all 17 required programs subject to A-133, which resulted in a savings exceeding \$250,000 to the City. During FY2013, the Audit Division will continue providing assistance by using internal resources exclusively.

While continuing to save the City audit fees by assisting in testwork, the mid and long-term goals have been to increase knowledge of the significant grant activities in which the City is involved and help the City achieve an assessment of a “low risk” entity, which reduces the required A-133 testing by 50%. Additionally, this becomes a mechanism that assists City Management in designing and developing a stronger internal control structure.



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### **ENTERPRISE RISK ASSESSMENT (ERA)**

**DESCRIPTION:** Each year the Audit Division develops the Audit Plan based upon risk (primarily business, financial, operational, etc.) Key benefits include; gains in significant knowledge, goodwill, and succession planning by having a diverse team exposed to all the major operations of the City. Professional auditing standards (both GAO and IIA) require audit resources to be allocated to projects based on continued risk assessment methodology. There are currently 4 major components to the ERA Process (1) Review of selected departments on a rotational basis, (2) Significant Events occurring during the FY, (3) Changes to major process, structure, leadership within the City, (4) Consideration of Information Systems.

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### **FOLLOW-UP PROCEDURES**

**DESCRIPTION:** As issues are identified during the course of conducting audits/engagements, they are documented and reported accordingly. In order to help initiate change and continued improvement, we communicate with responsible management at regular intervals, and obtain a status of progress on implementation of corrective actions. These communications are formally documented. Additionally, samples of items are tested on a periodic basis, depending on the magnitude, impact, and cost-savings with the results being published as formal reports assessing the remediation process.

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### **QUALITY ASSURANCE PROCEDURES**

**DESCRIPTION:** Professional standards require that the audit function have a system of quality control/assurance in place to ensure all necessary elements are in place and operating effectively. Each audit/project is reviewed by a professional staff not directly assigned to the audit. The goal is to verify that sufficient, appropriate evidence is gathered and documented do adequately support conclusions based on procedures that are designed to test relevant audit objectives (this includes consideration of Fraud, professional judgment, competency, and supervision).

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### **FRAUD HOTLINE/REPORTING**

**DESCRIPTION:** The Office of the City Controller provides two primary vehicles for reporting fraud, waste and/or abuse: (1) A Fraud Hotline answered by the Audit Division and (2) a link to report fraud available from both the Controller's Homepage and the Audit Division's Website. Additionally, the Audit Division provides auditing support based on requests from the OIG and/or other authorities. Each reported concern is addressed. This may result in performing substantive procedures, such as an audit, or may be referred to an outside agency or department for follow-up. The initial contact, work performed, conclusions and/or referral are documented to support their disposition. In some instances, this may also require subsequent follow-up or monitoring to adequately resolve. Consideration of Fraud Reporting is performed by the Audit Division on a regular basis and has direct involvement by professional staff that are Certified Fraud Examiners.



## DATA ANALYTICS AND CONTINUOUS AUDITING

**DESCRIPTION:** The Audit Division purchased computer software during FY 2009 that allows for data access, extraction, warehousing, and analysis. This system also provides the functionality of a computer assisted auditing tool (CAAT). The implementation began during the last quarter of FY 2009 and is continuing into FY 2013 based upon resource availability<sup>4</sup>.

The first phase of Continuous Auditing is integrating the tools capabilities within the Enterprise Resource Planning (ERP) environment. This has consisted of understanding the business process and how the information system captures and stores the relevant information. We have selected some procurement process transaction types that we are using as a basis to implement and advance this initiative. Other areas of are:

- Accounts Payable;
- Purchasing/Procurement Cards (P-Cards);
- Accounts Receivable; and
- Payroll.

Subsequent phases will detail more specific analytics tailored to City concerns of fraud, waste, and/or abuse, as well as perform analysis of other non-integrated systems. This will then allow our focus to be on identified performance measures and other potential anomalies for consideration of risk, contribution to the ERA, and support for future audit planning.

## UNANNOUNCED AUDITS

**DESCRIPTION:** The Audit Division may perform audits on an unannounced basis during the year. These may include:

- Compliance with Specific Administrative Procedures or Executive Orders
- Petty Cash Counts;
- Inventory Audits (Test Counts/Controls)

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<sup>4</sup> In order to continue successful implementation, the Audit Division needs to fill a current vacancy with the specialized skills to utilize CAATs.