



DATE: December 17, 2024

TO: City Council, Finance Committee, Darrel Pyle and Rick Knighton

FROM: Shaakira Calnick, City Auditor

SUBJECT: Office of the City Auditor Independence Impairment, Updates to Global Internal Audit Standards (the *Standards*) [Effective January 9, 2025], and Updates to the GAO's generally accepted government auditing standards (GAGAS) [Effective December 15, 2025]

I hope all is well. The Office of the City Auditor is garnering attention from states like Kansas and California. While this is great, it also increases the likelihood of scrutiny from other audit industry professionals. I wanted to notify you of topics that will be discussed in detail during the upcoming Finance Committee meeting. These topics include potential independence impairments, the internal audit charter, updates to Global Internal Audit Standards (the *Standards*), and updates to the GAO's Generally Accepted Government Auditing Standards (GAGAS).

Mayor Heikkila's suggested edits and modifications to the Internal Audit Charter have not been fully implemented. My commitment to the *Standards* and the Code of Ethics prohibits me from doing so without presenting the issue and potential safeguards to the Council, Finance Committee and the Norman public. Implementing some of these modifications could essentially render the City of Norman's internal audit function ineffective during the second year of its implementation. GAGAS 3.18 and 3.19 state: "In all matters relating to the GAGAS engagement, auditors and audit organizations must be independent from an audited entity. Auditors and audit organizations should avoid situations that could lead reasonable and informed third parties to conclude that the auditors and audit organizations are not independent and thus are not capable of exercising objective and impartial judgment on all issues associated with conducting the engagement and reporting on the work."

Comments regarding the suggested changes/edits are as follows:

Section 1. I am of the understanding that efforts to form an Audit Committee will occur in the future, as qualified at-large citizens with experience in the accounting/audit/risk fields seated on the Audit committee will enhance accountability and transparency within the City of Norman, as well as the awareness and understanding of the internal audit function. An audit committee safeguards organizational independence of the internal audit function and provides ongoing oversight, advice and feedback to the internal audit function. (Changed to "Interim Audit Committee").

Section 2. Adherence is the prerequisite of conformance. Without adherence, conformance may not be achievable. By “governing itself by adherence to” the Office of the City Auditor seeks to achieve conformance with the Standards. This section is the unmodified statement of commitment that must be present on all Internal Audit Charters in order to adhere, and conform with, the *Standards*. (This change will not be implemented.)

Section 3 (*Authority on pg. 3*). The City of Norman’s Office of the City Auditor’s authority is created by its direct reporting relationship to the City Council. Subject to the Oklahoma Open Meetings Act (O.S. Title 25, Sections 301-314), the City Auditor should be able to meet with members of Council or members of the Finance Committee (Interim Audit Committee) without management present. It is my understanding that a few Councilors meet with the City Manager on a periodic basis. Subject to the Open Meetings Act, this practice can be extended to the Office of the City Auditor. The Office of the City Auditor may conduct formal or informal one-on-one meetings with members of City Council to discuss the management, expectations, goals, and other matters related to the operations of the Office of the City Auditor. Meetings with members of City Council can be conducted one-on-one by phone, web-hosted video, email, or in person. Changes include acknowledgement of the Open Meetings Act, as well as available methods to conduct meetings between members of City Council and the City Auditor. Standard 6.3 (Board and Management Support) of Principle 6 (Authorized by the Board) of the Standards states: “The chief audit executive must provide the board and senior management with the information needed to support and promote recognition of the internal audit function throughout the organization. The chief audit executive must coordinate the internal audit function’s board communications with senior management to support the board’s ability to fulfill its requirements.” The essential conditions of this requirement are listed below:

Board

- Champion the internal audit function to enable it to fulfill the Purpose of Internal Auditing and pursue its strategy and objectives.
- Work with senior management to enable the internal audit function’s unrestricted access to the data, records, information, personnel, and physical properties necessary to fulfill the internal audit mandate.
- Support the chief audit executive through regular, direct communications.
- Demonstrate support by:
 - Specifying that the chief audit executive reports to a level within the organization that allows the internal audit function to fulfill the internal audit mandate.
 - Approving the internal audit charter, internal audit plan, budget, and resource plan.

- Making appropriate inquiries of senior management and the chief audit executive to determine whether any restrictions on the internal audit function's scope, access, authority, or resources limit the function's ability to carry out its responsibilities effectively.
- Meeting periodically with the chief audit executive in sessions without senior management present.

Senior Management

- Support recognition of the internal audit function throughout the organization.
- Work with the board and management throughout the organization to enable the internal audit function's unrestricted access to the data, records, information, personnel, and physical properties necessary to fulfill the internal audit mandate.

Section 3 (*Authority on pg. 3*). Council has previously approved R-2425-67, a resolution developed by the City Auditor, to create Policies and Procedures for the Office of the City Auditor. Policy Provision No. 4 states: "The City Auditor shall have access to, and perform examinations of, necessary documentation, policies, procedures, processes, staff, and facilities relevant to performing audit engagements (consultations, periodic audits, and fraud investigations) pursuant to Article III, Section 6, and Article V, Section 3 of the City of Norman Charter." The internal audit charter also acknowledges this. (Change: add "with Council's express approval by Resolution 2425-67)."

Due to resolution R-2425-67, requests for information (RFIs) should not have to go through the City Manager or Department Head. Additionally, their roles, actions, or lack thereof, are also assessed and evaluated during the audit engagement. Nevertheless, certain RFIs should and do go through the appropriate channels to adhere to laws, regulations, and the Standards. For instance, Human Resources (HR) and/or the City Attorney's Office may be consulted when acquiring access to certain employee records or when interviewing employees. When possible, Internal Audit works directly with employees who manage the records or files necessary to conduct the relevant audit, either through inquiry or request. Internal Audit does not exercise authority over any employee outside of the Office of the City Auditor.

Section 3 (*Independence, Organizational Position, and Reporting Relationships on pg. 3*).

Annually, internal auditors employed by the City of Norman's Office of the City Auditor will be required to sign the Annual Code of Ethics and Conflict of Interest Declaration, which will be retained in the Office of the City Auditor and in the employees' HR files. It may be excessive to report the organizational independence of the Office of the City Auditor semi-annually unless a situation arises. It is usually reviewed during the annual review of the Internal Audit Charter. Any other reporting frequency could negatively impact the productivity of the Office of the City Auditor.

Impairments that are identified must be communicated/reported promptly upon discovery. This disclosure should include only the Council, the Finance Committee, and other appropriate parties as deemed necessary.

Communication is continuous throughout the audit process with the appropriate parties. Audit reports are communicated to the City Manager, the appropriate Department Head, the Finance Committee, the City Council, and are published via the City of Norman website. Disclosure reports regarding interference related to scope, performance, or communications of internal audit work and results of internal auditing, performing work, and/or communicating results—and its implications on the Office of the City Auditor’s effectiveness—should be submitted to City Council and the Finance Committee. Any other arrangement could increase the likelihood of interference with the performance and/or completion of an audit or investigation and negatively impact the accountability and transparency of City operations. (For example, in efforts to achieve City objectives, the City Manager and Department Heads may unknowingly approve transactions and actions of employees that consequently violate City policy. Department Heads or the City Manager would have the ability to delay the audit process if they had the authority to approve or restrict the Office of the City Auditor’s ability to communicate such interference.)

Meetings between the Office of the City Auditor and employees of the City of Norman are coordinated through the Department Head of each department, as the City Manager has encouraged communication, coordination and collaboration with the Office of the City Auditor among employees of the City of Norman. (Essential Conditions for Senior Management of Standard 6.3: Board and Senior Management Support).

Section 4 (City Council Oversight). The word “sufficient” was removed.

According to the applicability and elements of the Standards, “may” and “should” specify common and preferred practices. These two words are essentially the same. No change is necessary here.

I have added the specific standard that lists the essential conditions to this bullet point, as it relates to Council Oversight.

Refer to Section 1 on all modifications to the Internal Audit Charter. The Finance Committee reviews the Internal Audit Charter for alignment with the City governance structure, and City Council approves the Internal Audit Charter.

The Internal Audit Charter is a living document, and City Council has the authority to review or approve the document annually—or not. It is best practice to list this as an authorized Council action in the Internal Audit Charter.

Providing input on the Office of the City Auditor’s Human Resource administration and budgets may be understood as a function of the City Manager’s office, but it is within the authority of the Council to support and approve budgets for additional audit employees as they relate to the Office of the City Auditor. Additionally, City Council is the only body authorized to appoint and remove the City Auditor. Thus, input from Council is inherently necessary concerning the hiring operations and hiring process of the Office of the City Auditor and the City Auditor.

“It is the authority of City Council to make appropriate inquiries of City Manager and the City Auditor to determine whether scope or resource limitations are inappropriate.” Mayor Heikkila seeks to change the entire statement to: “It is the authority of City Council to make appropriate inquiries of City Manager and the City Auditor to determine whether scope or resource limitations are appropriate,” which implies that senior management will have the authority to limit the scope of audits. This may cause another adverse effect on the independence of the internal audit function unless Council restricts the scope of internal audit services to a subset, according to certain criteria or a particular department or division, that they want audited on a periodic basis. It is within the authority of City Council to confirm that the Office of the City Auditor has the resources and access necessary to perform audits without interference. Internal audit services may be simply defined as in Article V, Section 3 of the City of Norman Charter, or may be specifically defined, such as performance audits, assurance regarding internal controls over financial reporting, and investigations. Scope restrictions should be explicitly outlined within Section 6, scope and types of internal audit services, of the Internal Audit Charter.

(Change: “Making appropriate inquiries of senior management and the chief audit executive to determine whether any restrictions on the internal audit function’s scope, access, authority, or resources limit the function’s ability to carry out its responsibilities effectively.”)

Section 5 (Ethics and Professionalism). Reporting administratively to Council or the Chair of the Finance Committee is another factor that may impair the independence of the internal audit function and may impact its effectiveness. Administrative reporting and approval of administrative requests should be limited to the City Manager, while functional reporting, as it relates to the operations of the Office of the City Auditor, is reserved for the Council and Finance Committee.

As it relates to ethics, encouraging and promoting an ethics-based culture is the responsibility of every City of Norman employee, not just the HR department. Standard 1.2 (Organization's Ethical Expectations) of Principle 1 (Demonstrate Integrity) of the Global Internal Audit Standards states: *"Internal auditors must encourage and promote an ethics-based culture in the organization."* and the considerations to implement this standard state, *"The internal audit plan may include assessments of the organization's ethics-related risks to determine whether existing policies and control processes adequately and effectively address those risks. The chief audit executive also should determine a methodology for addressing ethical issues and discuss the methodology with the board and senior management to ensure alignment of the approaches."*

Internal auditors should consider ethics-related risks and controls during individual engagements. If internal auditors identify behavior within the organization that is inconsistent with the organization's ethical expectations, they should communicate the concerns according to the methodology established by the chief audit executive, which takes into account the organization's policies and processes as well as laws and/or regulations.

If internal auditors determine that a member of senior management has behaved in a manner that is inconsistent with the organization's ethical expectations — whether documented in a code of conduct, code of ethics, or otherwise — the chief audit executive should report the violation to the board. If an ethics-related concern involves the chairman of the board, the chief audit executive should report the concern to the entire board.

Internal auditors should follow up on ethics-related issues involving the board or senior management and validate that appropriate actions were taken to address the concern."

Reporting organizational behavior that is inconsistent with the organization's ethical expectations (as described in policies and procedures) should be not reported to the City Manager (CM). Reporting organizational behavior that is inconsistent with the organization's ethical expectations (as described in policies and procedures) should be reported to the appropriate parties. Appropriate parties depend on the offender's level of employment. Internal Auditors are required to make such reports to the City Auditor who will review the report and determine a distribution list. All internal City policies are the responsibility of the CM. Therefore, the City Manager has the authority to override the City's policies and procedures. The City Auditor does not exercise authority over other Council employees or any City employee outside the Office of the City Auditor. Council is the only body with the authority to direct or instruct the CM.

Section 5 (*Objectivity, 3rd Paragraph*). This section details the ethical principle of objectivity of the Office of the City Auditor, lists situations that could impair that objectivity, and provides guidance on such matters. Essentially, it means the Office of the City Auditor should not perform any operational duties outside of the duties pertaining to the Office of the City Auditor. Impairments to internal auditors' objectivity have a direct impact on the independence of the Office of the City Auditor.

Changes: Added "Affiliates of the City of Norman (Norman Municipal Authority) include, but may not be limited to, the Norman Utilities Authority and Norman Tax Increment Finance Authority, outside contractors, and subcontractors."

Section 5 (*Managing the Office of the City Auditor*). Semi-annual updates of the triennial audit plan will not be implemented. Updates to the triennial audit plan are booklets prepared annually to provide updates on completed audits, ongoing audits, milestones reached, resources, etc. Semi-annual updates increase the likelihood that production would be negatively impacted. These updates are also published to the public via the City Auditor webpage on the City of Norman website.

Approval of communications or the ability to communicate with Council regarding significant interim changes to the triennial audit plan is not necessary. This may impact the City Auditor's access to the Board and Finance Committee as it relates to communicating any changes or updates to the triennial audit plan. Nevertheless, any changes implemented into the triennial audit plan require communication to Council and Council's approval. Senior management, including the City Manager, is included on the distribution list to receive the communications.

Changing "possess" to "possesses" would be incorrect grammar.

"Senior management" has been changed to "City Manager" where applicable.

Section 5 (*Communication with the City Council and Management*). This section includes a list of annual reports that are delivered to Council. Reporting semi-annually on the entire list may negatively impact the productivity of the internal audit function.

Changing "reporting potential impairments to independence" to "reporting potential impairments to operations" limits the intent of the statement in its entirety. Impairments to independence may result in an increased likelihood of interference in other areas, such as reporting, operations, and compliance.

Industry Standard Updates. Updates to Audit Industry Standards will affect the implementation of the Internal Audit function within the City of Norman. Updates to the IIA's Global Internal Audit

Standards will be effective January 9, 2025, and updates to the GAO's generally accepted government auditing standards (GAGAS) will be effective December 15, 2025. Specific updates have been implemented into the charter as it relates to the Internal Audit function in government. A PowerPoint presentation will be conducted to notify you in detail regarding the updated standards.