



CITY OF HAMILTON
CITY MANAGER'S OFFICE
Audit Services Division

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	October 13, 2015
SUBJECT/REPORT NO:	AUD15027 Evaluation of the Value For Money Pilot Program (City Wide) (Outstanding Business List Item)
WARD(S) AFFECTED:	City Wide
PREPARED BY:	Brigitte Minard 905-546-2424 x2088
SUBMITTED BY:	Brigitte Minard CPA, CA, CIA, CGAP Acting Director, Audit Services
SIGNATURE:	

RECOMMENDATION

- (a) That the 2.0 FTE temporary Performance Auditor positions become a permanent part of the Audit Services Division staffing complement when the Pilot Program ends on March 31, 2016.
- (b) That the 2016 budget for the Audit Services Division includes these 2.0 FTEs from April 1, 2016 onwards.
- (c) That the 2016 to 2018 Annual Audit Services Work Plan include consulting activities that enable and support the development of corporate-wide performance measures and continuous improvement initiatives.
- (d) That item (D) on the Audit, Finance & Administration Committee's Outstanding Business List, respecting the Value-for-Money Audit Program - End of Three Year Pilot, be considered complete and removed from the Outstanding Business List.

EXECUTIVE SUMMARY

The City's capacity and willingness to respond to recommendations arising from Value for Money (VFM) audits and implement changes and improvements to its practices is where the most significant benefits to taxpayers can be achieved. An organizational performance measurement system needs to be put in place so that the benefits can be measured, analysed and reported. When these benefits are measured and reported on a regular basis, this is where the true value to the organization is realized.

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Despite being identified as a priority in the SMT 2011 Work Plan, a performance measurement system does not exist at the organization-wide level at the City of Hamilton. While progress has been made as a result of the Service Delivery Review and projects executed by the Service Delivery Strategy Team, there still is not a performance measurement system and without such a system, it is challenging for the full benefits of VFM auditing to be realized, quantified and reported in a meaningful way.

Despite these challenges, many benefits have been realized during the course of the VFM Pilot Program, including the identification of \$798,000 in gross savings, along with many other non-financial recommendations made to improve efficiency and effectiveness throughout the organization along with addressing concerns relevant to the public.

There is a need for VFM auditing in the organization, however, the benefits will be greater to the organization in the long-term if there is an organizational performance measurement system in place that can support both management and VFM auditing.

Going forward, it is recommended that the 2.0 Performance Auditor FTEs be made permanent, with a different approach taken in the type of work completed for the remainder of the current Council term. This approach would include activities such providing advice, facilitation, education and training to enable the development an organization-wide performance measurement and continuous improvement system. Such activities would still be approved by Council as part of an Audit Services Annual Work Plan. Such activities are permitted in the Institute of Internal Auditors professional standards that the Audit Services Divisions adheres to and per the Council-approved Audit Services Charter (Report AUD15006).

Alternatives for Consideration – See Page 7

FINANCIAL – STAFFING – LEGAL IMPLICATIONS (for recommendation(s) only)

Financial: This request would shift funding for the Value for Money Auditing Program from reserve-based funding to levy-based funding.

Upon approval to add the VFM auditing component into Audit Services' permanent scope of work, additional annualized funding for staffing (salaries, benefits, software licenses and training) would be required and is estimated at approximately \$270,000. Additionally, it is prudent to include an annual budget of up to \$25,000 to allow for the retention of outside consultants in areas for which the Audit Services Division does not have expertise (e.g. engineering or environmental services). Therefore, the total ongoing, requested annualized increase in the Audit Services Division budget is approximately \$295,000.

Staffing: It is recommended that the 2.0 FTE Performance Auditor positions become permanent positions.

Legal: None.

HISTORICAL BACKGROUND (Chronology of events)

The pilot was set up after a motion at the March 21, 2012 GIC meeting to implement a Hybrid Auditor General model. The Director of Audit Services was directed to carry out a three year pilot project conducting VFM audits as approved by Council in the annual work plan.

The position of Director of Audit Services was designated an Auditor General (per the Municipal Act) through By-law 12-073. A significant role of an Auditor General (AG) is to conduct VFM audits. These audits are compliance and operational reviews combined with a component to assess whether or not the City has obtained benefit from the goods and services it acquires and provides.

Direction was given to report back through the Audit, Finance and Administration Committee at the conclusion of each audit with the results and recommendations, and annually to identify tangible savings/increased revenues, if any realized, as a result of the implementation of recommendations in the year. Also, direction was given to report back at the end of the pilot, summarizing the estimated cumulative savings, in addition to highlighting the non-financial benefits such as improved internal controls, operational efficiencies and environmental, social or service improvements, as appropriate, resulting from the VFM program.

On March 18, 2013, the Value for Money Audit Program pilot commenced. There was a delay between the VFM Program pilot start date and approval from GIC, due to issues encountered in recruiting qualified staff for the program (detailed in Report AUD12019 from October 2012).

The requirement to report annually to identify tangible savings/increased revenues and annually was fulfilled with Report AUD14012 for the first year of the program.

A report was not provided to AF&A in early 2015 as the DARTS review was directed by Council and therefore there were no VFM projects to summarize and report. Additionally, funding for the complete duration of the VFM pilot was approved at the May 12, 2014 AF&A meeting, so the need for annual reporting was lessened.

This report fulfils the requirement to report back at the end of the VFM pilot, summarizing estimated cumulative savings and highlighting non-financial benefits.

Pilot Program Challenges

Other Requests from Council and Staffing Issues:

Both Performance Auditors (the only staff in the VFM pilot program) were reassigned full time to complete the DARTS Review, per the direction of Council. As a result of this reassignment, no resources were available to complete VFM work for a 12-month period. Council also requested one month (of 1.0 FTE's time) to complete a review of Hamilton Police Service Issues and one month (of 1.0 FTE's time) to do consulting work on the Cash Handling Guidelines.

Also, one of the two Performance Auditors initially hired in March 2013 resigned in September 2014, this position remained vacant for 4 months.

Therefore, as of August 31, 2015, the 2.0 temporary FTE Performance Auditor positions have been available to perform VFM work for 14.5 of 29.5 months (about 50%) of the time initially allocated for the pilot program. With both positions currently filled, if there are no additional Council requests or vacancies until the end of the pilot program in March 2016, the Performance auditors will have had 22.5 of the 36 months initially allocated to focus on VFM work. This represents about 60% of the time initially allocated to the pilot program, this is significantly less time than originally intended for the pilot program and the reduced timeframe has had an impact on the volume of work generated by the VFM pilot.

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

In 2012, By-law 12-073 designated the Director of Audit Services as an Auditor General per the Municipal Act. There are no additional policy and legislative implications at this time. The Director of Audit Services continues to be designated as an Auditor General per the Municipal Act.

RELEVANT CONSULTATION

- The City Manager, Director of Corporate Initiatives, Director of Corporate Communications and Intergovernmental Affairs and Finance & Administration staff were consulted during the report writing process.
- The Institute of Internal Auditors IPPF (professional standards) were reviewed.
- The City Auditor from the City of Burlington was consulted with.

**ANALYSIS AND RATIONALE FOR RECOMMENDATION
(Include Performance Measurement/Benchmarking Data if applicable)**

To continue to deliver the benefits and pilot program accomplishments noted above it is recommended that the VFM program become a permanent part of the Audit Services Division and that the 2.0 FTEs perform consulting activities with a focus on enabling Continuous Improvement initiatives (including the development of performance measures) in the short to medium term (to the end of the current Council term). This approach will enable the long-term success VFM auditing and enable the organization to effectively deliver services to taxpayers.

Need for VFM Auditing in the Organization:

The work of the Audit Services Division encompasses the examination and evaluation of the adequacy and effectiveness of the City's governance, risk management process, system of internal control structure and the quality of performance in carrying out assigned responsibilities to achieve the organization's goals and objectives. This currently includes conducting VFM audits. VFM recommendations enable the City's processes to function in a manner that ensures:

- Significant financial, managerial and operating information is accurate, reliable and timely.
- Actions are in compliance with policies, standards, procedures and applicable laws and regulations.
- Resources are acquired economically, used efficiently and are adequately protected.
- Programs, plans and objectives are achieved.
- Quality and continuous improvement are fostered in the organization's control processes.

Pilot Program Accomplishments

The gross savings identified during the pilot program are estimated to be \$798,000 (for projects completed as at July 31, 2015). However, the implementation of many of the recommendations in the VFM reports will require expenditures to make the needed changes to implement the recommendations. Total net savings are unable to be fully quantified as not all costs to achieve these savings are known at this time, the actual savings will be lower than the estimated savings. For a detailing listing of the pilot program's accomplishments, refer to Appendix A of this report. The cost of the pilot program as at July 31, 2015 was \$537,000.

Many other non-financial recommendations were made in the VFM audit reports to improve efficiency and effectiveness throughout the organization and address concerns relevant to the public, including:

- Implementing electronic funds transfers which may result in more timely payments to City suppliers;

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- Eliminating unfair advantages for those businesses who choose to operate without a license;
- Better utilization of GPS/AVL systems to manage staff productivity and efficiency;
- Creating performance metrics to measure performance and monitor workflow (in the area of claims adjusting); and
- Limiting the number of pre-printed agendas available to the public to reduce waste (in the Office of the City Clerk).

Next Steps:

As previously identified in report CM11006/AUD11028, to successfully undertake VFM auditing, an organizational performance measurement system is needed. Presently, such a system does not exist at the organization-wide level at the City of Hamilton. For the organization to support full VFM auditing, a consistent and organizational-wide approach to reviewing its services and performance is required. This was identified as a priority in the SMT 2011 Work Plan.

It has been a consistent finding in internal audit projects and one VFM audit that there is a lack of performance measures in the organization. Management is ultimately responsible and accountable for organizational performance. However, it would be of great value to the organization for the VFM FTEs to temporarily enable the development of performance measures as part of an ongoing Continuous Improvement initiative rather than continue to audit in an environment that has a lack of performance measures. It is important that an organizational performance measurement system be in place to enable VFM auditing (per Report CM11006). This type of audit is difficult to conduct because the methodology (i.e. focus on inputs/effort, process, and outputs/effect) is not in alignment with how the organization is currently managed.

Transitioning the organization to one that includes consistent and meaningful performance measurement will be a significant cultural change for the organization. A shift towards performance measurement and continuous improvement would be in alignment with the Corporate Culture Pillars-Courageous Change, Collective Ownership and Sensational Service.

Performance Auditors have the knowledge, skills and expertise to support the development of corporate-wide performance measures and continuous improvement initiatives. VFM auditing includes evaluating processes and recommending improvements related to economy, efficiency and effectiveness. Performance measurement and benchmarking skills have been utilized in the completion of VFM audits during the pilot program.

Realization of Savings

Performance measures are a challenging concept to introduce consistently across an organization. This will require a significant change to the way business is currently conducted in the organization and will also be a major cultural change.

Validation of Identified Savings

The achievement of savings identified in the VFM audit reports have not been validated with a Follow Up VFM audit. This is due to the fact that there was a focus on identifying savings during the pilot program, along with the fact that staff resources have been diverted for approximately 50% of the VFM pilot program to date.

Shifting Back to VFM Auditing in the Long-Term

After focusing on performance measurement and continuous improvement activities, effort would shift back to VFM auditing. VFM auditing would resume in a more integrated fashion. The Audit Services Annual Work Plan for 2019 onwards would include some VFM audits, or individual audit project scopes may include VFM components (e.g. evaluating economy, efficiency and effectiveness). The Audit Services Annual Work Plan going forward would be comprehensive, risk-based plan that would include compliance, control and VFM audit work. Results and summaries of all VFM activities would continue to be reported to the A,F&A Committee as the projects are completed.

Focus on Low-Hanging Fruit

The initial focus of the program was on “low-hanging fruit” to produce quick wins for the program. While this approach was successful and did identify savings (as documented in Appendix A), these projects are not true VFM audits. A true VFM audit with the potential to identify significant savings can take at least six months to complete. The length of the pilot program made it important to focus on quick wins rather than projects that may have taken longer, but had higher potential to transform the organization.

ALTERNATIVES FOR CONSIDERATION

(Include Financial, Staffing, Legal and Policy Implications and Pros and Cons for each alternative)

- 1) The 2.0 FTE temporary Performance Auditor positions become a permanent part of the Audit Services Division staffing complement when the Pilot Program ends on March 31, 2016.

Financial: This request would shift funding for the Value for Money Auditing Program from reserve-based funding (Tax Stabilization Reserve) to levy-based funding.

Upon approval to add the value-for-money (VFM) auditing component into Audit Services’ scope of work, additional annualized funding for staffing (salaries, benefits, training, equipment and supplies) would be required and is estimated at approximately \$270,000. Additionally, it is prudent to include an annual budget of \$25,000 to allow for the retention of outside consultants in areas for which the Audit Services Division does not have expertise (e.g. engineering or environmental services).

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Therefore, the total ongoing, requested annualized increase in the Audit Services Division budget is approximately \$295,000.

Staffing: It is recommended that the 2.0 FTE Performance Auditor positions become permanent positions.

Legal: None.

Pros:

- Addresses the need for an organization-wide performance measurement system.
- Provides VFM auditing for the organization long-term.
- Utilizes in-house resources primarily.
- Has the potential to change the organization for the better in the long-term.

Cons:

- Requires the addition of 2.0 permanent FTEs.
- Adds additional funding pressure to the general levy.

This is the recommended option. The benefits to the organization far outweigh the costs. The VFM pilot program identified more savings than the pilot costs, the pilot has been providing good value to the organization and is expected to continue to do so. This option is in the best interest of taxpayers in the long-term.

2) Extend the Value for Money Pilot Program by a minimum of 15 months with funding from the same reserve fund (Tax Stabilization Reserve) as the pilot program.

This would allow the pilot program to function for a 36-month period as originally intended. It is suggested the same reserve fund be utilized as the funding source for the extended pilot program.

The estimated incremental one-time cost for this option is approximately \$182,000. (The gross cost is \$296,000; however there is \$114,000 of unspent reserve funds that were approved for the Pilot Program). The unspent funds represent approximately 5 months' worth of funding. The program would be re-evaluated at the end of this extended Pilot Program.

Financial: One-time incremental cost of \$182,000.

Staffing: 2.0 temporary FTE (Performance Auditors) positions are extended for a 15-month term concluding in June 2017.

Legal: None.

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Pros:

- Allows VFM auditing to continue for 15 months and provide recommendations to the organization.

Cons:

- Extension is only on a temporary basis, there will not be a significant positive long-term benefit to the organization. There will not be the opportunity for any large VFM projects to be undertaken and there may not be time to identify significant savings during the extension of this pilot program.
- This option does not address the need for an organization-wide performance measurement system.
- Staffing the program for contract positions has been challenging in the past and is not expected to change for the foreseeable future.

This alternative is not recommended.

3) Incorporate VFM auditing into the Audit Services Division.

VFM auditing techniques could be incorporated into the work that is performed by the current staff in the Audit Services Division. The permanent staff in the Division consists of 7.0 FTEs (1.0 Director, 1.0 Supervisor, 4.0 Auditors and 1.0 Administrative Assistant). It is the 4.0 auditor positions that are primarily responsible for completing audit projects.

The Annual Audit Work Plan for 2016 onwards could include some VFM audits, or individual audit project scopes could include VFM components (i.e. economy, efficiency and effectiveness). The Annual Audit Work Plan would continue to be a comprehensive, risk-based plan that would include compliance and control audits with the addition of VFM audit work. In order to appropriately staff the Division for the addition of VFM work to the work plan, it is recommended that 1.0 permanent FTE be hired.

This FTE would be a Senior Internal Auditor-all staff at this level would be expected to incorporate VFM principles and concepts into their audit projects. It is also recommended that the \$25,000 consulting budget that existed during the pilot program continue as this allows the Audit Services Division to continue to access external expertise as-needed for projects that have components that are not in the scope of in-house expertise (e.g. engineering or environmental expertise). The total annual cost for this option is \$159,000 (\$134,000 of staffing costs and \$25,000 consulting budget).

Financial: Annual cost of \$159,000 (\$134,000 staffing and \$25,000 consulting).

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Staffing: 1.0 permanent FTE (Senior Internal Auditor) is added, 2.0 temporary FTE (Performance Auditors) positions are eliminated.

Legal: None.

Pros:

- VFM continues in the organization on a limited basis.
- Request is for 1.0 permanent FTE rather than 2.0 FTEs.

Cons:

- Not as high a volume of VFM can be completed by 1.0 permanent FTE rather than 2.0 FTEs during the VFM pilot.
- Requires the addition of 1.0 permanent FTE.
- Adds additional funding pressure to the general levy.
- This option does not address the need for an organization-wide performance measurement system.
- Training will need to be provided to the existing 2.0 FTE Senior Internal Auditors

This alternative is not recommended.

4) Committee and Council can decide not to support the Value for Money Audit Program any longer. No funding past the cancellation date would be required and the two temporary Performance Auditor positions would be eliminated.

However, VFM auditing could be incorporated into the regular audit work that is performed by the Audit Services Division. Value for Money auditing techniques would be incorporated into the work that is performed by the current staff in the Audit Services Division. The permanent staff in the Division consists of 7.0 FTEs (1.0 Director, 1.0 Supervisor, 4.0 Auditors and 1.0 Administrative Assistant). The 4.0 auditors perform the bulk of the audit fieldwork.

The Audit Services Annual Work Plan for 2016 onwards would include some VFM audits, or individual audit project scopes may include VFM components (i.e. economy, efficiency and effectiveness). The Audit Services Annual Work Plan going forward would continue to be a comprehensive, risk-based plan that would include compliance, control and VFM audit work. The total volume of work of the Division would decrease due to the removal of the 2.0 temporary Performance Auditor FTE's, but a limited amount of VFM work would continue to be completed.

It is also recommended that the \$25,000 consulting budget that existed during the pilot program continue as this allows the Audit Services Division to continue to access external expertise as-needed for projects (i.e. engineering or environmental expertise). Total annual cost for this option is \$25,000.

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Financial: \$25,000 annual cost (for consulting).

Staffing: 2.0 Temporary FTE positions are eliminated (no levy savings as these 2.0 FTE's were funded from reserves).

Legal: None.

Pros:

- This is a low-cost option that allows for some limited VFM auditing to continue occurring in the organization.
- No permanent FTE's added to the organization.
- Annual increase to the levy is minimal.

Cons:

- A reduced number of VFM projects, along with a reduced number of internal audit projects will be performed by the Division due to the loss of the dedicated 2.0 employees supporting the VFM function and the work being performed by a smaller number of staff.
- The resources utilized to train staff in the VFM pilot program will not be fully utilized.
- This option does not address the need for an organization-wide performance measurement system.
- Existing staff in the Audit Services Division would need to be trained in VFM techniques.

This alternative is not recommended.

ALIGNMENT TO THE 2012 – 2015 STRATEGIC PLAN

Strategic Priority #1

A Prosperous & Healthy Community

WE enhance our image, economy and well-being by demonstrating that Hamilton is a great place to live, work, play and learn.

Strategic Objective

1.6 Enhance Overall Sustainability (financial, economic, social and environmental).

Strategic Priority #2

Valued & Sustainable Services

WE deliver high quality services that meet citizen needs and expectations, in a cost effective and responsible manner.

Strategic Objective

- 2.1 Implement processes to improve services, leverage technology and validate cost effectiveness and efficiencies across the Corporation.
- 2.2 Improve the City's approach to engaging and informing citizens and stakeholders.
- 2.3 Enhance customer service satisfaction.

Strategic Priority #3

Leadership & Governance

WE work together to ensure we are a government that is respectful towards each other and that the community has confidence and trust in.

Strategic Objective

- 3.2 Build organizational capacity to ensure the City has a skilled workforce that is capable and enabled to deliver its business objectives.
- 3.3 Improve employee engagement.
- 3.4 Enhance opportunities for administrative and operational efficiencies.

APPENDICES AND SCHEDULES ATTACHED

Appendix "A" to AUD15027 – Summary of Identified Savings

Appendix "B" to AUD15027 – Audit Services Division Organizational Chart

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