



To: New Castle County Audit Committee
From: Bob Wasserbach
Subject: Audit Plan for First Half of Fiscal Year 2019¹
Date: June 5, 2018

Audit Plan/Schedule – July 2018 through December 2018 (may carry over into second half of Fiscal Year 2019)

The County Government is currently experiencing budgetary difficulties and has been drawing down on its reserves for several years. If the County continues on its current path, the Property Tax Stabilization Reserve and the Sewer Rate Stabilization Reserve are projected to reach \$0 in Fiscal Year 2019. Also, the “Rainy Day” reserves for the General and Sewer funds are projected to reach \$0 in Fiscal Years 2021 and 2020, respectively. The depletion of these reserves is likely to negatively affect the County’s AAA bond rating and its ability to borrow at a low cost in the bond market.²

Because of this, we plan on concentrating on those audits/projects that we believe have the potential to increase revenues and/or decrease expenses to the County. Please be aware, however, that a large portion of the County’s budget is in salaries & wages and most of this expense item is driven by the union contracts.

Planned Audits

- **Fleet Operations: Complete this audit which was on the prior Audit Plan.**
- **Real Estate Transfer Taxes (RTT), concentrating on controls over claimed exemptions. The budget for RTT for Fiscal Year 2019 is approximately \$31 million. This audit will include:**
 - **There is a form that must be completed to claim an exemption from the real estate transfer tax. There are a myriad of exemptions that can be claimed so as to not pay this tax. The Recorder of Deeds Office receives these forms and does not really do anything with them except to file them. The ultimate control over ensuring the person is eligible for the claimed exemption is apparently the review by the attorney handling the transaction and the fact that the person signing the form does so under penalty of perjury. We plan on obtaining a general understanding of the number of exemptions by exemption category and, for the higher dollar categories, determining whether there is anything the County should be doing to determine the individual’s right to the exemption.**
 - **There are County Code restrictions on (1) what percentage of estimated transfer tax proceeds may be utilized in the annual operating budget, (2) what actual transfer tax revenues up to that percentage can be utilized for, and (3) how funds received in excess of that percentage can be spent. We will evaluate whether the County is in compliance with these Code provisions.**
 - **We will evaluate the controls over the collection of transfer taxes by the Recorder of Deeds Office, the remittance of the revenues to the County, and the proper recording of the revenues.**
- **Land Use Fees (e.g., building permit fees, subdivision review fees, business license fees). We have never audited the fees associated with the Land Use Department, which are approximately \$10**

¹ May carry over into second half of fiscal year.

² As of the date of this memorandum, the Fiscal Year 2019 budget, which contains additional revenues so as to reduce the amounts to be taken from County reserves in FY '19 and future years, has not yet been approved by County Council.

million a year (not including capital recovery fees which we previously covered on our Sewer Connection Fees audit.) We will evaluate the controls over the calculation, collection and recording of these fees.

- **Health Insurance, concentrating on the controls over claims processing. The County is self-insured and spends over \$50 million a year in employee benefits (of which a large majority is for employee health care). We have never audited this high-dollar area. The audit will focus on ensuring the County is not paying for any medical expenses it shouldn't be. We will consider hiring a specialist to assist us on this audit.**
- **Construction Contracts including Responsible Contractor Compliance: The County Code states "The County or a using agency or a county agency shall require any person proposing to bid on a special services contract, as a condition to submitting a bid to it for consideration, to submit to the Office of Administrative Services a Contractor Responsibility Certification for contracts where the probable cost of the contract is expected to exceed five hundred thousand dollars (\$500,000.00)." A couple of Council Members have expressed concerns on whether certain bidders who are awarded County contracts are in full compliance with the elements of the Contractor Responsibility Certification. This audit will evaluate contractor compliance with the County Code requirements. The audit will also review a sample of construction projects to (1) ensure the bids were awarded in accordance with County Code and Procurement's Policies & Procedures Manual and (2) that the project was managed properly (including proper support for payments and compliance with policies and procedures for change orders).**

We will also:

- Continue to coordinate the external audits of the County's and Pension Fund's financial statements and the audit of the County's compliance with federal grant requirements.
- As time permits, work closely with the County CFO and his key staff on a few projects:
 - Replacement for County's Tier Financial System: Provide input on the features desired in the new system and ensure the new system has adequate internal controls. Explore ways to utilize our data analytics software package in new system, e.g., for continuous auditing responsibilities.
 - Local service function: This is the annual process in which the Office of Finance requests incorporated municipalities in New Castle County (NCC) to complete an application form regarding governmental services provided by the municipality which NCC does not need to provide itself. The completion of the application allows residents of the municipality to receive County property tax relief for those services provided by the municipality. The new CFO has been analyzing Finance's process for providing these property tax credits to ensure the County is not leaving revenue "on the table", i.e., residents in these municipalities are paying their fair share to NCC. The CFO will be providing us with updates on this project.
 - Consideration of moving from annual to monthly billing for sewer service fees: The County Administration is now considering this; as such, we want to ensure (if this happens) that adequate internal controls are established over the process.
 - Lodging Tax: If the State grants NCC the authority to charge a lodging tax, and if County Council passes legislation to enact the tax, work with the Office of Finance to ensure that the County implements adequate internal controls over the collection and recording of this tax.
 - Assessments: The Office of Finance has worked hard to reduce the backlog of assessment appeals. In anticipation of possibly including an Assessments audit on our next Audit Plan, we may do some research and documentation on the assessments appeals process.
- Prepare for a Peer Review of the County Auditor's Office.

In addition to the above items, the County Auditor's Office has set aside hours to review any County-Government-related items that arise during the period that the County Auditor deems worthy of review. Such items arise from County Council meetings, requests from Council Members or the public, current events, the Auditor's professional skepticism, etc. If the County Auditor decides to review an item that is not reflected in the above plan, he will notify the Executive Office and County Council in writing that he will be reviewing such item. Upon notification of such review, the item officially becomes a part of the Audit Plan. If the item will take more than 100 hours, the County Auditor will ask the Audit Committee for approval to formally amend the Audit Plan.

This Audit Plan/Schedule, once approved by the Audit Committee, will be submitted to the County Executive, County CAO, and County Council. Any amendments to the Plan/Schedule will be provided to the same parties.

Relevant Authority

Delaware State Code, Title 9, Chapter 14, § 1407 Audit schedule; special examinations or audits; risk assessment review.

“(a) Prior to the beginning of each fiscal year, the County Auditor shall submit an annual audit plan to the Audit Committee for review and comment. The plan shall include the proposed schedule for auditing departments, offices, boards, activities, agencies and subcontractors for the period. The plan and schedule may be amended during the period after consultation with the Audit Committee. The schedule and any amendments shall be provided to the Council and the County Executive.”

Due to the constantly evolving nature of County Government, the County Auditor’s Office has chosen to present an Audit Plan for six-month periods.

Please note that the County Auditor’s Office is comprised of the County Auditor, a Staff Auditor, and a Part-Time Senior Staff Auditor. This staffing level is less than the auditing departments of many municipalities of comparable size. Thus, we are not able to audit as many areas each year as we’d like to be able to.

Generally Accepted Government Auditing Standards

GAGAS 1.01 states: “The concept of accountability for use of public resources and government authority is key to our nation’s governing processes. Management and officials entrusted with public resources are responsible for carrying out public functions and providing service to the public effectively, efficiently, economically, ethically, and equitably within the context of the statutory boundaries of the specific government program. The U.S. Government Accountability Office’s (GAO’s) auditing standards, commonly referred to as generally accepted government auditing standards (GAGAS), provide a framework for conducting high quality audits with competence, integrity, objectivity, and independence. Such standards help to improve government operations and services.”

GAGAS 6.03: “In performance audits that comply with GAGAS, auditors obtain reasonable assurance that evidence is sufficient and appropriate to support the auditor’s findings and conclusions in relation to the audit objectives.”

The majority of the audits performed by the County Auditor’s Office are performance audits designed to determine whether internal controls provide reasonable assurance regarding the achievement of management’s objectives relating to operations, reporting, and compliance.

Standards for Internal Control in the Federal Government

Internal control helps an entity run its operations efficiently and effectively, report reliable information about its operations, and comply with applicable laws and regulations. The publication *Standards for Internal Control in the Federal Government*, known as the “Green Book,” sets the standards for an effective internal control system for federal agencies. The Green Book states “The Green Book provides managers criteria for designing, implementing, and operating an effective internal control system.”

The Green Book incorporates COSO’s (Committee of Sponsoring Organizations of the Treadway Commission’s) “Internal Control – Integrated Framework” for identifying the internal controls management has implemented to help accomplish its objectives. See “Internal Control – Integrated Framework” Executive Summary.

Although the Green Book is not required to be utilized by local governments, arguments for utilizing it in New Castle County Government are as follows:

- The Green Book states: “The Green Book may also be adopted by state, local, and quasi-governmental entities, as well as not-for-profit organizations, as a framework for an internal control system.”
- The GFOA (Government Finance Officers Association) issued a Best Practice in September 2015, titled “Internal Control Framework”, stating “The GFOA recommends that state and local governments adopt the COSO’s *Internal Control—Integrated Framework* (2013) as the conceptual basis for designing,

implementing, operating, and evaluating internal control so as to provide reasonable assurance that they are achieving their operational, reporting, and compliance objectives. To implement that guidance, a government needs to:

1. Establish a comprehensive framework for internal control that includes *all five essential components* identified by the COSO (control environment, risk assessment, control activities, information and communication, and monitoring);
 2. Ensure that each component of internal control is functioning in a manner consistent with *all relevant principles*; and
 3. Ensure that the various components complement one another and operate together effectively.
- The GFOA (Government Finance Officers Association) issued a Best Practice in September 2015, titled “Internal Control for Grants”, which states “The most widely recognized source of guidance on internal control is the Committee of Sponsoring Organizations (COSO), which updated its classic *Internal Control—Integrated Framework* in 2013. The GFOA has organized the following best practice steps for grant internal control into COSO’s five essential components of a comprehensive framework of internal control: 1) Control Environment; 2) Risk Assessment; 3) Control Activities; 4) Information and Communication; and 5) Monitoring.”
 - Federal regulations (CFR 200.303) require recipients of federal grants to “Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in ‘Standards for Internal Control in the Federal Government’ issued by the Comptroller General of the United States and the ‘Internal Control Integrated Framework’, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The County’s external auditors, as part of the June 30, 2015 audit, issued a management letter comment recommending “The County should review its current policies and procedures to ensure they have incorporated best practices from these frameworks.” (i.e., the Green Book and COSO)
 - A KPMG webinar, titled “Green Book Implementation – Leading Practices for State and Local Governments” recommended the Green Book and COSO as best practices.

New Castle County management has not implemented the Green Book (and thus COSO) to design and implement its internal control system. This is not to say that management has not designed and implemented internal controls, only that it has not been using the Green Book methodology.

However, we intend to use the Green Book methodology in evaluating the adequacy of internal controls over the functions that we audit.