

**By-laws of the
Internal Audit Board
of the
Lexington-Fayette Urban County Government
Adopted April 12, 2011
Amended May 3, 2016**

Section

- I. Purpose
- II. Meetings
- III. Attendance
- IV. Performance
- V. Board Training
- VI. Quorum and Motion Votes
- VII. Conflicts of Interest
- VIII. Board Membership
- IX. Non-Disclosure Agreement
- X. Requests for Confidential Information
- XI. Conflicts of Interests – Department of Law
- XII. Fraud Allegations
- XIII. Closed Sessions
- XIV. Special Audit Requests
- XV. Rights and Duties of the Board
- XVI. Board Self-Examination
- XVII. Membership of the Board
- XVIII. Modifications to By-laws

LFUCG Internal Audit Board By-laws

I. Purpose-

The Internal Audit Board (Board) is an independent body established by the LFUCG to govern and ensure that the Office of Internal Audit (OIA) complies with the Code of Ethics and Professional Standards (Standards) of the Institute of Internal Auditors (IIA) in fulfilling its duties to provide assurance and consulting services designed to add value and improve LFUCG's operations, and to ensure that the OIA assists LFUCG in accomplishing its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. The LFUCG Internal Audit By-laws address Board governance, the independence of the Board from the Administrative and Legislative branches of the LFUCG, issues of confidentiality, and performance rights and duties.

II. Meetings-

The Board shall conduct regular meetings with specific scheduled dates/times being established annually by the Board. In no event shall the Board meet less than quarterly. Regular meetings may be cancelled upon authorization by the Board Chair or Acting Chair. Special meetings of the Board shall be called as deemed necessary by the Board Chair or Acting Chair. Regular meetings and special meetings shall be announced and held in compliance with Kentucky Open Meetings laws. The Chair or Acting Chair shall develop and set the meeting agenda in consultation with the Director of Internal Audit and other members of the Board. Board Members may suggest the inclusion of items on the agenda. The agenda and information concerning the business to be conducted at each meeting shall, to the extent practical, be communicated to the members of the Board two business days in advance to permit meaningful review.

III. Attendance-

Board members are expected to attend Board meetings. Board members shall give the Chair at least a two business day advance notice if they are unable to attend a Board meeting. Absences from four regular meetings within a calendar year shall result in a Board recommendation to the Urban County Council for removal of the Board member. The Board Chair or Acting Chair shall notify a Board member when he or she had three (3) absences within a calendar year.

IV. Performance-

Board members shall review the IIA Code of Ethics and Standards and the LFUCG Code of Ethics, and are expected to conform to the Codes' standards of business conduct. The Director of Internal Audit shall conduct an orientation of the IIA Code of Ethics and Standards, the LFUCG Code of Ethics, and Office of Internal Audit policies and governing documents, and procedures for new members. Board members are expected to self-report any potential violations of or conflicts with the Codes to the Board Chair. Failure to comply with performance requirements may result in a Board recommendation for removal of the Board member.

V. Board Training-

The Board shall request presentations and other training regarding internal audit practices, emerging issues, and LFUCG financial, operational, and compliance processes and functions as deemed necessary by the members of the Board to fulfill their governance duties. The Director of Internal Audit shall provide Board members with a copy of all current Statutes, Ordinances or Resolutions related to the Board and its activities.

VI. Quorum and Motion Votes-

A simple majority of the voting members of the Board shall constitute a quorum. The approval of Board meeting minutes and any actions taken by the Board shall require a vote. A simple majority of voting members present, if a quorum is established, shall constitute approval of the minutes or motion being voted on. A tie vote of voting members present shall result in a failed approval of a motion.

VII. Conflicts of Interest-

Board members are required to avoid any real or apparent financial or personal conflicts of interest while serving on the Board. At the beginning of each calendar year, Board members shall complete a financial disclosure form and shall be responsible for updating the information on this form when appropriate during the year. The Director of Internal Audit shall facilitate this process. Financial conflicts of interest are defined by the LFUCG Code of Ethics. Board members shall recuse from any discussions or votes wherein they have a real or the appearance of a Conflict of Interest. Failure to comply with Conflict of Interest requirements may result in a Board recommendation for removal of the Board member.

VIII. Board Membership-

1. Membership on the Board shall be in conformance with LFUCG ordinances governing the appointment and removal of members to or from the Board. The Board shall have the authority to communicate issues of attendance, performance,

conflicts of interest, failure to adhere to the Non-Disclosure Agreement or other breeches of confidentiality, or other non-compliance with the Board By-laws to the Urban County Council and to recommend the removal of a Board member.

2. A recommendation to remove a Board member shall require a motion and a majority vote of the Board. The Board member whose removal is being considered shall not be allowed to vote. If the removal motion passes, the Chair of the Board shall notify the Urban County Council in writing within five (5) business days.

IX. Non-Disclosure Agreement-

Board members shall sign a Non-Disclosure Agreement requiring them to keep confidential the contents of any and all audit workpapers they examine for any and all audit projects unless they have a legal or professional obligation to share the contents of certain workpapers as stipulated by law and/or IIA Standards. When the question of legal obligation arises, a legal opinion shall be provided to the Board by its legal counsel and the Board shall then make a determination of how to proceed after its review of the legal opinion. The decision shall be formalized by a Board vote.

X. Process to Communicate to the Board Requests Received by the Office of Internal Audit for Confidential Information or Audit Workpapers-

Any requests received by the OIA for information deemed confidential or that otherwise involve audit workpapers shall be promptly communicated to the Board. In considering such requests the Board shall obtain the legal advice of counsel as necessary, shall comply with the Standards, and shall consider the impact releasing workpapers would have on the OIA's ability to fulfill its duties to the LFUCG. The decision shall be formalized by a Board vote. The Board shall take guidance from 10-ORD-164 issued on August 20, 2010 by the Kentucky Office of the Attorney General and any subsequent updates, rulings or decisions by Kentucky Courts regarding the confidentiality of audit workpapers.

XI. Seeking Legal Counsel When Department of Law has a Conflict of Interest-

If the Board or the Director of Internal Audit has a reasonable belief that the LFUCG Department of Law has a real or apparent conflict of interest in advising the Board or the OIA regarding legal matters, the Board, upon majority vote, shall seek advice from outside legal counsel.

XII. Process for Addressing Fraud Allegations Brought to the Attention of the Office of Internal Audit or the Board-

1. Any and all fraud allegations brought to the attention of the OIA or a member of the Board shall be communicated to the full Board as promptly as possible. To confidentially accomplish such notice, the Board member or OIA shall promptly inform the Board Chair, who shall promptly inform the remaining Board members using the most efficient means of communication available. This may include the use of regular meetings, special meetings, phone calls, e-mail, or other methods as deemed necessary. If the fraud allegation involves the Board Chair, the Vice-Chair shall be the first contact for the person receiving the fraud allegation. If the allegations of fraud involve a member of the Board, this member shall recuse from any vote regarding the investigation of the matter, and shall fully cooperate with the Board and the OIA in the vetting of the allegations. Failure to provide full cooperation may result in a Board recommendation for removal of the Board member. Any concerns brought to the attention of the OIA or the Board that do not allege fraud shall be addressed in the **Special Audit Requests** section XIV of the By-laws. The fraud tip line or any other fraud reporting processes developed by the LFUCG shall report all allegations of fraud to the OIA and the Board, and shall be subject to governance by the Board. The Board will utilize the definition of occupational fraud as defined by the Association of Certified Fraud Examiners.

2. All allegations of fraud shall be given due consideration. The OIA shall initiate a preliminary review of all fraud allegations it receives using IIA Standards and Code of Ethics and Association of Certified Fraud Examiners (ACFE) Standards and Code of Ethics, including the ACFE fraud predication standards. In order to ensure the allegations are fully vetted under these professional standards, a full investigation may or may not be necessary depending on the results of the preliminary review. Using guidance from these professional standards, the Director of Internal Audit shall exercise professional judgment regarding the extent to which such an investigation should be conducted. The Director of Internal Audit shall inform the Board of the results of all investigations alleging fraud. The use of closed sessions to discuss allegations of fraud with the Board in Board meetings shall be exercised in compliance with the Closed Session section of the Bylaws.

3. In any circumstances where the applicability of the Kentucky Open Meeting and Open Records laws are in question, the Board shall seek legal advice before determining what, if any, action is appropriate. The Board will be informed of all open records requests.

4. The Board shall communicate the results of fraud investigations to the Administration and/or Council if circumstances dictate a need to know by one or both parties. Need to know shall be interpreted as a fraud investigation resulting in the need for further action on the part of the Administration and/or Council. A preliminary review resulting in a determination that no credible evidence of fraud exists shall not, as a matter of practice, be considered a need to know situation. However, members of the Administration and Council are encouraged to bring any questions about fraud allegations to the Board, which in consultation with the Director of Internal Audit, shall provide information regarding the vetting of fraud allegations. Administration and Council requests for information about preliminary investigations that did not find credible evidence of fraud, and therefore as a matter of practice are not considered a need to know situation, shall be considered by the Board on a case-by-case basis.

5. The Board Chair or designee (also a Board member) shall keep a log of all fraud allegations and will work with the Director of Internal Audit to track the status of the vetting process. This tracking will also occur when the allegations are assigned to another Division within the LFUCG (e.g., Human Resources).

6. Board members shall keep confidential any and all allegations of fraud brought to the attention of the Board until a preliminary or full investigation of those allegations have been completed by the OIA and the results of that investigation have been released. Board members shall then restrict their comments about the investigation to the contents of any released reports. Breach of the confidentiality requirements of this section of the By-laws may result in a Board recommendation for removal of the Board member.

XIII. Closed Session-

As allowable under Kentucky Open Meetings laws, the Board may go into closed session to discuss allegations of fraud that may result in the disciplinary action of an LFUCG employee, or to discuss pending litigation involving the Board or the OIA. The OIA and/or the Board will consult with legal counsel regarding the use of closed sessions.

XIV. Special Audit Requests-

1. A Special Request for audit services is defined as a formal request from LFUCG Administration, Council, or LFUCG staff employees for an examination of processes or functions within the LFUCG and related entities receiving LFUCG funding or oversight. Although a special request may include fraud allegations, it may also be a request for a standard or limited scope audit service to be inserted in the Approved

Audit Plan. A Special Request may be in writing or verbal, and should provide to the extent practicable the nature of the request and the specific areas of concern. If originally received verbally, a written version will be requested for presentation to the Board. A Special Request may be received by either the OIA or the Board.

2. Any and all Special Requests brought to the attention of the OIA or a member of the Board shall be communicated to the full Board as promptly as possible. To accomplish this, the Board member or OIA shall promptly inform the Board Chair, who shall promptly inform the remaining Board members. This may include the use of regular meetings, special meetings, phone calls, e-mail, or other methods as deemed necessary. If a Special Request involves allegations of fraud, it shall be addressed using the processes defined in Section XII **Fraud Allegations**. Once received, the Board shall review the Special Request with the Director of Internal Audit.

3. If the Board determines that the OIA should examine a Special Request (and it does not allege fraud), the Board shall determine via a vote when to conduct the preliminary review of the Special Request, unless the Board determines that the nature and clarity of the Special Request is such that a preliminary review is not needed, in which case the Board may vote to insert the Special Request into the Annual Audit Plan or to take no further action on it. If directed by the Board, a preliminary review shall be conducted using IIA and ACFE standards, including ACFE standards used to determine fraud predication if the Special Request alleges fraud.

4. If a preliminary review is conducted, the Director of Internal Audit shall report to the full Board the results of the preliminary review and his recommendations. The Board shall then vote to insert the Special Request into the Annual Audit Plan or to discontinue further review. The results of that vote shall then be communicated by the Board to the individual making the Special Request, if known.

XV. Rights & Duties of the Board-

The rights and duties of the Board shall include -

1. The periodic review of the performance of the Director of Internal Audit, who reports directly to the Board. The annual performance appraisal of the Director of Internal Audit will be conducted by the Chief Administrative Officer (CAO) with input from and approval by the Board prior to being submitted to the Division of Human Resources. Any performance issues regarding the Director of Internal Audit (who is a Classified Civil Servant) shall be addressed in full compliance with the

Comprehensive Plan for Classified Civil Service System, and shall also require Board approval formalized by a vote in order to proceed;

2. At least annually in a written report, review the organizational structure, qualifications, independence, objectivity, and performance of the OIA and the scope of its planned activities;
3. In ensuring the independence and objectivity of the OIA, shall have authority to establish policies to address any threats or perceived threats to its independence or objectivity, including scope and resource limitations;
4. At least annually, formally review the Board's organizational structure and Board members' financial disclosure forms to ensure the independence and objectivity of the Board;
5. **Review and approve the Internal Audit Charter annually, and amend the Charter as needed to ensure continued conformity with the Institute of Internal Auditors' Definition of Internal Auditing, the Standards, and the Code of Ethics.**
6. Periodically review the OIA Procedure Manual and offer recommended changes if needed;
7. Discuss with the Director of Internal Audit any areas of risk the external auditors bring to the Director's attention and how that risk may be mitigated through internal audit services. Meet at least once annually with the external auditors as needed to accomplish this duty;
8. Approve the annual audit plan and any amendments to the audit plan;
9. Annually examine the resource and staffing needs of the OIA, and approve its annual budget;
10. Review all reports issued by the OIA, along with management's action plan to address audit findings and any necessary follow-up processes designed to ensure implementation of action plans;
11. Supervise the Director of Internal Audit in the conduct of his operational responsibilities, while ensuring the Director of Internal Audit reports administratively to the CAO;

12. Annually review the OIA to ensure its compliance with IIA Standards;
13. Authority to engage in-house legal counsel or other advisors as needed to fulfill the duties of the Board or the OIA;
14. Authority to obtain independent legal counsel when addressing matters that may create a conflict of interest for employees within the Department of Law. This authority shall extend to the Board having the right to obtain additional financial resources from the LFUCG to obtain such legal counsel if necessary;
15. Authority to access LFUCG's books and records (regardless of media) as well as management and other personnel records as needed to discharge the duties of the Board or the OIA;
16. Review the independent assessment of the OIA function on a five year basis as required by the IIA Standards.
17. To instruct the Director of Internal Audit to periodically report audit findings and other issues to the Council's Budget & Finance Committee or other council committees as requested by the Urban County Council.
18. The authority to bring to the attention of senior management and/or the Council any circumstances or incidents wherein there is credible evidence an employee of the LFUCG willfully provided misleading information or willfully withheld requested information as the result of audit-related inquiries made by OIA personnel or members of the Board.

XVI. Board Self Evaluation-

The Board shall annually review its own performance for compliance with the IIA Standards and other audit board governance standards and best practices, including Board independence and objectivity. The Board shall include a report of its annual self-evaluation in the Board meeting minutes, and deliver a copy to the Clerk of the Council to publish digitally on the LFUCG's website.

XVII. Membership of the Board-

The membership of the Board shall comply with the requirements of applicable LFUCG Ordinances creating the Board and its duties, and any amendments thereof. This shall include the requirement that the Board Chair and Vice-Chair be voting

Board members selected from the community, in order to enhance Board independence. Board rotation and term limits shall comply with the requirements of applicable LFUCG Ordinances and any amendments thereof.

XVIII. Modifications to the By-laws-

From time to time, the Board may adopt changes or modifications to the By-laws by majority vote. Any such changes will be submitted to the Urban County Council for review and approval.