



Item 4.2: Review and Approval of Internal Audit Department Charter

Penny Rychetsky
Director of Internal Audit

Finance & Audit Committee Meeting

ERCOT Public
February 11, 2020

Review and Approval of Internal Audit Department Charter

- Required periodic review of the Internal Audit Department Charter.
- Internal Audit is not recommending changes to the current charter.
- Attached is the current charter (Attachment A) last approved by the Finance and Audit Committee on February 11, 2019.



Internal Audit Department Charter

MISSION, PURPOSE AND SCOPE

The mission of Internal Audit is to enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight. Internal Auditing is an independent, objective assurance and consulting activity designed to add value and improve the organization's operations. It helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

The Internal Audit Department is an independent function established within the Electric Reliability Council of Texas (ERCOT) to plan, develop and perform internal auditing activities. In support of ERCOT's Strategic Objectives, the Internal Audit Department provides management with recommendations for improving operations through assurance and consulting services. Assurance services are an independent and objective examination of evidence to ensure risk management, control, and governance processes are adequate and functioning in an appropriate manner. Consulting services are advisory in nature and may include facilitation, training and advisory services. The audit plan may include assurance activities, consulting engagements and special projects.

PROFESSIONAL STANDARDS AND PROCEDURES

Internal Audit Department activities are conducted in accordance with mandatory guidance including the Code of Ethics and the *International Standards for the Professional Practice of Internal Auditing*, promulgated by the Institute of Internal Auditors. In addition, the Internal Audit Department will adhere to ERCOT's policies and procedures and Internal Audit's Department Guide.

The Chief Audit Executive (CAE) will annually assess whether the responsibility and authority, as defined in this charter, continue to be adequate to enable the Internal Audit Department to accomplish its objectives. The result of this annual assessment will be communicated to executive management and the Finance and Audit Committee (Committee) of the Board of Directors.

The Internal Audit Department will be subject to the required external quality assurance review every five years in accordance with professional standards. Additionally, an internal continuous monitoring assessment program provides assurance of adherence to auditing standards, staff training requirements and job performance expectations. The CAE must communicate the results of the quality assurance and improvement program to senior management and the board.

INDEPENDENCE, OBJECTIVITY AND AUTHORITY

To ensure independence of the Internal Audit Department, the CAE reports administratively to the Chief Executive Officer (CEO) and functionally to the Committee. The CAE serves at the pleasure of the CEO and the Committee.

The CAE enhances independence and meets the Institute of Internal Auditors' *Standard* requirement of communication and direct interaction with the board through periodic meetings with the Committee. The CAE confirms the organizational independence of the department with the Committee on an annual basis.

The Internal Audit Department has no direct authority over the activities under review. Internal auditors should not be assigned duties or engage in any activities they would normally be expected to review since performance of these operational duties might compromise their objectivity. Examples include implementing internal controls, developing procedures, installing systems, preparing records, directing employees not employed by the Internal Audit Department, or engaging in any other activity that would normally be audited. Objectivity is essential to properly fulfilling internal audit responsibilities.

Internal auditors shall be granted unlimited access to all activities, employees, property, and records related to audit activities. Though such access shall be unlimited, the internal auditors shall ensure the safekeeping and confidentiality of all records and information in their possession. The Internal Audit Department also has full and free access to the Committee and the authority to conduct audits independently and without interference to accomplish audit objectives.

ACCOUNTABILITY

The Director of Internal Audit is the CAE at ERCOT. The CAE, in the discharge of his/her duties, shall be accountable to the CEO and the Committee to:

- Periodically provide information on the status and results of audit work, the annual audit plan, and the sufficiency of department resources, and
- Coordinate with executive management in the development of an annual risk assessment, and audit plan that effectively addresses issues of control, risk management, and governance processes.

KEY ROLES AND RESPONSIBILITIES

Key roles and responsibilities of the CAE, Committee, CEO and executive management are critical to the success of the internal audit function. The CAE will assist the CEO and executive management in the identification and management of company risks.

Key responsibilities of the Chief Audit Executive include:

- Developing an effective internal auditing program based on a flexible, risk-based annual audit plan, and submitting the plan to the Committee for review and approval;
- Implementing the approved annual audit plan including all assurance and consulting projects;
- Effectively communicating the results of audit projects;
- Providing periodic status reports of the audit plan and results to the CEO and the Committee;

- Working with the CEO and Committee to assess the budget and staffing levels of the Department;
- Maintaining a professional audit staff with sufficient knowledge, skills, experience, and professional certifications;
- Establishing a quality assurance program by which the CAE assures efficient and effective performance of internal auditing activities; and
- Conducting investigations at the direction of the Committee Chairman and the Committee.

Key responsibilities of the Finance and Audit Committee include:

- Approving the Internal Audit Department Charter annually;
- Providing any input and approving the risk-based Annual Internal Audit Plan;
- Reviewing the Internal Audit Department budget and resource plan;
- Approving the selection of the external quality assurance reviewer every five years;
- Reviewing internal audit reports;
- Receiving communications from the CAE on the Internal Audit Department's performance relative to its plan and other matters;
- Approving decisions regarding the appointment and removal of the CAE;
- Consulting with the CEO regarding the remuneration of the CAE; and
- Inquiring of management and the CAE to determine whether there are inappropriate scope or resource limitations.

Key responsibilities for the Chief Executive Officer include:

- Initiating the recruitment and hiring of a qualified CAE/Internal Audit Director;
- Ensuring the independence of the internal audit function through establishment of an organizational structure with direct lines of reporting between the CAE and the CEO;
- Assessing the Internal Audit Department's budget and staffing levels in coordination with the CAE for Board approval;
- Performing an annual evaluation of the CAE;
- Reviewing and accepting internal audit reports;
- Contributing to and reviewing the results of the risk assessment prepared to support the annual internal audit plan;
- Reviewing the Internal Audit Charter; and
- Communicating with the CAE regarding issues or concerns pertaining to internal audit activities.

Key responsibilities for executive management include:

- Cooperating with audit teams during the performance of internal audits by granting unlimited access to all activities, employees, property and records requested by the auditors;
- Reviewing internal audit reports and providing written responses to address issues and recommendations, and ensuring corrective actions are taken or accepting the associated risk; and
- Providing information to auditors regarding the occurrence and status of significant issues, which pertain to the organization and its risks.

Penny V. Rychetsky
Chief Audit Executive

Bill Magness
President and Chief Executive Officer

Terry Bulger
Finance and Audit Committee Chairman

Dated

DRAFT