

California High-Speed Rail Authority

Internal Audit Charter

Purpose

The purpose of the internal audit function is to strengthen the Authority's ability to create, protect, and sustain value by providing the Board and management with independent, risk-based, and objective assurance, advice, insight, and foresight.

The internal audit function enhances the Authority's:

- Successful achievement of its objectives.
- Governance, risk management, and control processes.
- Decision-making and oversight.
- Reputation and credibility with its stakeholders.
- Ability to serve the public interest.

The Authority's internal audit function is most effective when:

- Internal auditing is performed by competent professionals in conformance with The Institute of Internal Auditors' (IIA) Global Internal Audit Standards, and U.S. Government Accountability Office (GAO) Generally Accepted Government Auditing Standards (GAGAS), which are set in the public interest.
- The internal audit function is independently positioned with direct accountability to the Board.
- Internal auditors are free from undue influence and committed to making objective assessments.

Commitment to Adhering to the Audit Standards

The Authority's internal audit function will adhere to the mandatory elements of the audit standards. The Chief Auditor will report periodically to the Board and senior management regarding the internal audit function's conformance with the Standards, which will be assessed through a quality assurance and improvement program.

The Audit Office shall adhere to the following professional standards:

- Global Internal Audit Standards by The Institute of Internal Auditors, as applicable.
- Government Auditing Standards (GAGAS) by the Comptroller General of the United States, as applicable.

- Other professional standards as recommended or required by the Office of Audits and Evaluations (Department of Finance), the California State Auditor and/or other State control agencies that may be applicable.

Mandate: The Audit Office provides objective evaluations, opinions and recommendations concerning operational and programmatic deficiencies and internal and external risks to the organization; strategies for managing organizational risks; and optimization of the internal control environment.

The Authority's internal audit function mandate is found in following:

- Public Utilities Code section 185000 to 185012 – “California High-Speed Rail Act”.
- Government Code section 13885 to 13888– “Internal Audits”.
- California State Administrative Manual, Chapter 20000: Section 40 “Internal Audit Organizations”; Section 50 “Audit Standards”; Section 60 “Internal Control”; and Section 70 “Reporting Risks, Internal Controls, and Monitoring”.
- Government Code sections 13400 to 13407 – “State Leadership Accountability Act”.

The internal audit function's authority is created by its direct reporting relationship to the Board. Such authority allows for unrestricted access to the Board.

The Board authorizes the internal audit function to:

- Review, identify risks, and make recommendations for risk mitigation in all areas of the Authority's operations.
- Have full and unrestricted access to all functions, data, records, information, physical property, and personnel pertinent to carrying out internal audit responsibilities. Internal auditors are accountable for confidentiality and safeguarding records and information.
- Allocate resources, set frequencies, select subjects, determine scopes of work, apply techniques, and issue communications to accomplish the function's objectives.
- Obtain assistance from the necessary personnel of the Authority and other specialized services from within or outside the Authority to complete internal audit services.

Independence, Organizational Position, and Reporting Relationships

The Chief Auditor will be positioned at a level in the organization that enables internal audit services and responsibilities to be performed without interference from management, thereby establishing the independence of the internal audit function (see

“Mandate” section). The Chief Auditor will have direct and unrestricted access to senior management and the Board. The Chief Auditor will report functionally to the Board and administratively to the Authority’s Chief Executive Officer (CEO). This positioning provides the organizational authority and status to bring matters directly to senior management and escalate matters to the Board, when necessary, without interference and supports the internal auditors’ ability to maintain objectivity.

The Chief Auditor will confirm to the Board, at least annually, the organizational independence of the internal audit function. If the governance structure does not support organizational independence, the Chief Auditor will document the characteristics of the governance structure limiting independence and any safeguards employed to achieve the principle of independence. The Chief Auditor will disclose to the Board any interference internal auditors encounter related to the scope, performance, or communication of internal audit work and results. The disclosure will include communicating the implications of such interference on the internal audit function’s effectiveness and ability to fulfill its mandate.

It is the responsibility of the Audit Office to conduct reviews, examinations, assessments, evaluations, and audits, collectively audits of the Authority’s program and administrative control systems to determine if the control systems are operating in accordance with management’s instructions, policies, and procedures, and in a manner which supports the attainment of strategic goals and objectives. In addition, the Audit Office is responsible for:

- Reporting the results of audits to management personnel of sufficient authority to ensure that appropriate action is taken with respect to any deficiency noted.
- Assessing management’s action plans proposed to correct reported conditions. If an action plan is considered unsatisfactory, it is the responsibility of the Audit Office to conduct further discussions with program and executive management to achieve satisfactory resolution.
- Coordinating external audit activities.
- Submitting annual audit plans to the Board and CEO for review, approval, and reporting regularly on progress toward implementation of annual plans.
- Reporting to the Board and CEO as to whether appropriate action has been taken on audit findings; whether audit activities have been directed toward the areas of highest exposures to risk with an emphasis on increasing efficiency, economy, and effectiveness of operations and attainment of program objectives; whether internal and external audits are coordinated to avoid duplication; whether audit plans are adequate; and whether there are any restrictions to access.

- Reporting to the appropriate state entity any audit findings that may be considered material and/or egregious and reporting to the Board and CEO.
- Reporting to the appropriate division chiefs to provide an update on corrective actions and to notify them of any uncorrected deficiencies in their respective operational areas.
- The Chief Auditor is responsible for convening quarterly meetings of the CEO and appropriate division chiefs of any uncorrected findings or conditions included in the audit follow-up allowing the CEO to better ensure prompt corrective action by all responsible parties.

Charter Updates

Circumstances may justify a follow-up discussion between the Chief Auditor, the Board, and senior management on the internal audit mandate or other aspects of the internal audit charter. If warranted by significant changes, the charter will be updated accordingly. Such circumstances may include but are not limited to:

- A significant change in the Audit Standards.
- A significant reorganization within the organization.
- Significant changes in the Chief Auditor, the Board, and/or senior management.
- Significant changes to the organization's strategies, objectives, risk profile, or the environment in which the organization operates.
- New laws or regulations that may affect the nature and/or scope of internal audit services.

Board Oversight

To establish, maintain, and ensure that the Authority's internal audit function has sufficient authority to fulfill its duties, the Board will:

- Discuss with the Chief Auditor and senior management the appropriate authority, role, responsibilities, scope, and services (assurance and/or advisory) of the internal audit function.
- Ensure the Chief Auditor has unrestricted access to and communicates and interacts directly with the Board, including in private meetings without senior management present in accordance with applicable laws and regulations. Discuss with the Chief Auditor and senior management other topics that should be included in the internal audit charter.
- Participate in discussions with the Chief Auditor and senior management about the "essential conditions," described in the Global Internal Audit Standards, which establish the foundation that enables an effective internal audit function.

- Approve the internal audit function's charter, which includes the internal audit mandate and the scope and types of internal audit services.
- Review the internal audit charter periodically with the Chief Auditor to consider changes affecting the organization, such as the employment of a new chief audit executive or changes in the type, severity, and interdependencies of risks to the organization; and approve the internal audit charter.
- Approve the risk-based internal audit plan.
- Provide input to the internal audit function's human resources administration and budgets.
- Review significant fluctuations to the internal audit function's budget and expenditures.
- Provide input to senior management on the appointment and/or removal of the Chief Auditor, ensuring adequate competencies and qualifications and conformance with the Global Internal Audit Standards.
- Review and provide input to senior management on the Chief Auditor's performance.
- Receive communications from the Chief Auditor about the internal audit function including its performance relative to its plan.
- Ensure a quality assurance and improvement program has been established and review the results annually.
- Make appropriate inquiries of senior management and the Chief Auditor to determine whether scope or resource limitations are inappropriate.

Chief Auditor Roles and Responsibilities

Ethics and Professionalism

The Chief Auditor will ensure that internal auditors:

- Conform with the Audit Standards, including the principles of Ethics and Professionalism: integrity, objectivity, competency, due professional care, and confidentiality.
- Understand, respect, meet, and contribute to the legitimate and ethical expectations of the organization and be able to recognize conduct that is contrary to those expectations.
- Encourage and promote an ethics-based culture in the organization.
- Report organizational behavior that is inconsistent with the organization's ethical expectations, as described in applicable policies and procedures.

Objectivity

The Chief Auditor will ensure that the internal audit function remains free from all conditions that threaten the ability of internal auditors to carry out their responsibilities in an unbiased manner, including matters of engagement selection, scope, procedures, frequency, timing, and communication. If the Chief Auditor determines that objectivity may be impaired in fact or appearance, the details of the impairment will be disclosed to appropriate parties.

Internal auditors will maintain an unbiased mental attitude that allows them to perform engagements objectively such that they believe in their work product, do not compromise quality, and do not subordinate their judgment on audit matters to others, either in fact or appearance.

Internal auditors will have no direct operational responsibility or authority over any of the activities they audit. Accordingly, internal auditors will not implement internal controls, develop procedures, install systems, or engage in other activities that may impair their judgment, including:

- Assessing specific operations for which they had responsibility within the previous year.
- Performing operational duties for the Authority or its affiliates.
- Initiating or approving transactions external to the internal audit function.
- Directing the activities of any the Authority employee that is not employed by the internal audit function, except to the extent that such employees have been appropriately assigned to internal audit teams or to assist internal auditors.

Internal auditors will:

- Disclose impairments of independence or objectivity, in fact or appearance, to appropriate parties and at least annually, such as the Chief Auditor, the Board, management, or others.
- Exhibit professional objectivity in gathering, evaluating, and communicating information.
- Make balanced assessments of all available and relevant facts and circumstances.
- Take necessary precautions to avoid conflicts of interest, bias, and undue influence.

Managing the Internal Audit Function

The Chief Auditor has the responsibility to:

- At least annually, develop a risk-based internal audit plan that considers the input of the Board and senior management. Discuss the plan with the Board and senior management and submit the plan to the Board for review and approval.
- Communicate the impact of resource limitations on the internal audit plan to the Board and senior management.
- Communicate with the Board and senior management if there are significant interim changes to the internal audit plan.
- Review and adjust the internal audit plan, as necessary, in response to changes in the Authority's business, risks, operations, programs, systems, and controls.
- Ensure internal audit engagements are performed, documented, and communicated in accordance with the Audit Standards and laws and/or regulations.
- Follow up on engagement issues/findings and confirm the implementation of recommendations or action plans and communicate the results of internal audit services to the Board and senior management periodically and for each engagement as appropriate.
- Ensure the internal audit function collectively possesses or obtains the knowledge, skills, and other competencies and qualifications needed to meet the requirements of the Audit Standards and fulfill the internal audit mandate.
- Identify and consider trends and emerging issues that could impact the Authority and communicate to the Board and senior management as appropriate.
- Consider emerging trends and successful practices in internal auditing.
- Establish and ensure adherence to methodologies designed to guide the internal audit function.
- Ensure adherence to the Authority's relevant policies and procedures unless such policies and procedures conflict with the internal audit charter or the Audit Standards. Any such conflicts will be resolved or documented and communicated to the Board and senior management.
- Coordinate activities and consider relying upon the work of other internal and external providers of assurance and advisory services. If the Chief Auditor cannot achieve an appropriate level of coordination, the issue must be communicated to senior management and if necessary escalated to the Board.

Communication with the Board and Senior Management

The Chief Auditor will report periodically to the Board and senior management regarding:

- The internal audit function's mandate.
- The internal audit plan and performance relative to its plan.
- Internal audit budget.
- Significant revisions to the internal audit plan and budget.
- Potential impairments to independence, including relevant disclosures as applicable.
- Results from the quality assurance and improvement program, which include the internal audit function's conformance with Audit Standards and action plans to address the internal audit function's deficiencies and opportunities for improvement.
- Significant risk exposures and control issues, including fraud risks, governance issues, and other areas of focus for the Board that could interfere with the achievement of the Authority's strategic objectives.
- Results of assurance and advisory services.
- Resource requirements.
- Management's responses to risk that the internal audit function determines may be unacceptable or acceptance of a risk that is beyond the Authority's risk appetite as identified in the Authority's Strategic Plan.

Quality Assurance and Improvement Program

The Chief Auditor will develop, implement, and maintain a quality assurance and improvement program that covers all aspects of the internal audit function. The program will include external and internal assessments of the internal audit function's conformance with the Audit Standards, as well as performance measurement to assess the internal audit function's progress toward the achievement of its objectives and promotion of continuous improvement. The program also will assess, if applicable, compliance with laws and/or regulations relevant to internal auditing. Also, if applicable, the assessment will include plans to address the internal audit function's deficiencies and opportunities for improvement.

Annually, the Chief Auditor will communicate with the Board and senior management about the internal audit function's quality assurance and improvement program, including the results of internal assessments (ongoing monitoring and periodic self-assessments) and external assessments. External assessments will be conducted at

least once every three years by a qualified, independent assessor or assessment team from outside the Authority; qualifications must include at least one assessor holding an active Certified Internal Auditor credential for engagements that were completed in compliance with Global Internal Audit Standards.

Scope and Types of Internal Audit Services

The scope of internal audit services covers the entire breadth of the organization, including all the Authority's activities, assets, and personnel. The scope of internal audit activities also encompasses but is not limited to objective examinations of evidence to provide independent assurance and advisory services to the Board and management on the adequacy and effectiveness of governance, and control processes for the Authority.

The nature and scope of advisory services may be agreed with the party requesting the service, provided the internal audit function does not assume management responsibility. Opportunities for improving the efficiency of governance, risk management, and control processes may be identified during advisory engagements. These opportunities will be communicated to the appropriate level of management.

The scope of work of the Audit Office is to determine whether the operational and administrative environment is in conformance with the Authority's values and goals and is adequate to ensure that:

- Programs are operating within the highest fiduciary standards and in accordance with applicable laws and approved policies.
- Programs and processes are consistent with governmental best practices.
- Legislative and/or regulatory issues are recognized and addressed appropriately.
- Operations and processes are consistent with the values and goals.
- Existing policies and procedures are appropriate and updated.
- Risks within and outside of the Authority are appropriately identified and managed.
- Financial, managerial, and operating information is accurate, reliable, and timely.
- Resources are acquired economically, used efficiently, and adequately protected.
- Contractors are meeting the objectives of their contracts, while in conformance with applicable laws, regulations, policies, procedures, and best practices.
- Responsibilities and activities of internal auditors are coordinated with those of external auditors to avoid duplication of efforts.

- Appropriate access for auditors and investigators of the state and federal governments is provided.
- Specific operations, processes or programs are reviewed at the request of the Board or Chief Executive Officer (CEO).

The Audit Office performs the following types of audits and reviews:

- Performance
- Compliance
- Financial-related
- Advisory
- Investigative
- Information Technology
- Follow-Up

Internal audit engagements may include evaluating whether:

- Risks relating to the achievement of the Authority's strategic objectives are appropriately identified and managed.
- The actions of the Authority's officers, directors, management, employees, and contractors or other relevant parties comply with the Authority's policies, procedures, and applicable laws, regulations, and governance standards.
- The results of operations and programs are consistent with established goals and objectives.
- Operations and programs are being carried out effectively, efficiently, ethically, and equitably.
- Established processes and systems enable compliance with the policies, procedures, laws, and regulations that could significantly impact the Authority.
- The integrity of information and the means used to identify, measure, analyze, classify, and report such information is reliable.
- Resources and assets are acquired economically, used efficiently and sustainably, and protected adequately.

Approval

The Audit Charter is transmitted to the Chair of the Board and is effective upon approval on the date indicated below.

Acknowledgments/Signatures

Paula Rivera, Chief Auditor

Date

Tom Richards, Chair, Board of Directors

Date

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