

S U M M A R Y M I N U T E S

REGULAR MEETING OF THE AUDIT OVERSIGHT COMMITTEE
ORANGE COUNTY, CALIFORNIA



Wednesday, February 27, 2013, 1:00 p.m.

HALL OF ADMINISTRATION
333 Santa Ana Blvd., 5th Floor
Conference Room A
Santa Ana, California

Supervisor Shawn Nelson
Chairman of the Board
AOC Chairman

Supervisor Patricia Bates
Vice-Chairman of the Board
AOC Member

Jan Grimes
Chief Deputy Auditor-Controller
AOC Member

Shari L. Freidenrich
Treasurer-Tax Collector
AOC Member

Robert J. Franz Interim County Executive Officer

Steve Danley
Interim Performance Audit Director
Ex-Officio AOC Member (non-voting)

Dr. David Carlson
AOC Vice-Chairman, Public Member

Sarah J. "Sally" Anderson

Mark Wille

Public Member

Bruce Hughes
Public Member

ATTENDANCE: Shawn Nelson, Pat Bates, Jan Grimes, Shari Freidenrich, Bob Franz, Bruce Hughes, Steve Danley, Mark Wille, David Carlson

EXCUSED: Sally Anderson

PRESENT: Director of Internal Audit Dr. Peter Hughes, CPA
County Counsel: Ann Fletcher
Clerk: Renee Aragon

1:02 P.M.

1. Roll Call

Attendance of AOC members is noted above.

Internal Audit staff – Mike Goodwin, Alan Marcum, Eli Littner, Michael Dean; Auditor-Controller Staff – Greg White, Autumn McKinney Claire Moynihan, Denise Steckler, Ila Patel; Second District Staff – Lindsay Brennan; Fourth District Staff – David Zenger; External Auditors Vavrinek, Trine & Day – David Showalter, Kevin Pulliam, Roger Alfaro; Treasurer-Tax Collector Staff – Paul Gorman; Grand Jurors – Fred Bennet, John Costello.

2. Approve Audit Oversight Committee regular meeting minutes of November 7, 2012

Motion-Franz, Second-Nelson, Yes-Grimes, Yes-Freidenrich, Yes-B. Hughes, Abstain-Bates, Abstain-Wille, Excused-Anderson

Approved as Recommended

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3. Approve Audit Oversight Committee special meeting minutes of December 20, 2012

Motion-Grimes, Second-Franz, Yes-Nelson, Yes-Freidenrich, Yes-B. Hughes, Abstain-Bates, Abstain-Wille, Excused-Anderson

Approved as Recommended

4. Receive Required Communication from External Auditors Vavrinek, Trine, Day & Company, LLP

Mr. Kevin Pulliam, Partner, Vavrinek, Trine, Day & Co., presented the required communications to the Audit Oversight Committee.

Mr. Pulliam stated the Single Audit was on-going and dealt with the federal expenditures. The number of programs audited range from seven to 18. It was anticipated the audit would be completed in the end of March 2013 and the results would be presented at the next AOC meeting. Mr. Pulliam stated there were no difficulties in performing the audit; however, there were some misstatements and adjustments that were identified and corrected. He said management signed a representation letter for each report issued. There was no consultation or opinions sought with other auditors that they were aware of.

Mr. Roger Alfaro, Partner, Vavrinek, Trine, Day & Co., reported on the corrected misstatements and adjustments. He stated the misstatements were presented to management and reported in the CAFR. The misstatements were identified according to reporting unit. Adjustments 1 through 5 dealt with the CAFR.

The first adjustment identified pertained to the recognition of receivables and revenues at June 30, 2012 to the extent that a receivable was accrued but the money was not collected soon enough to be used to liquidate current obligations. The adjustment was made to reflect diverted revenue.

The second adjustment noted for \$56 million pertained to a reclassification of equity within the financial statements. The adjustment did not have an impact on the income statement or on the assets or liabilities but was just a classification of equity.

The third adjustment was a result of information released from the State Controller's Office related to Health and Welfare Realignment Revenue. The communication was issued late October 2012 after the County's closing process. Management posted the adjustment for amounts due to the County but wasn't expected to be paid until the subsequent fiscal year.

The fifth adjustment for approximately \$170 million related to cash and investments reported within the investment trust fund.

Adjustments six, seven, eight and nine were as a result of enabling legislation in the fiscal year related to the dissolution of the Redevelopment Agencies. An audit was performed on the former OCDA as of January 31, 2012. Misstatements were detected related to timing. The agency ceased to exist as of January 31, 2012 and the County should have gone through a process of amending identified transactions that should have been attributed to the former OCDA as opposed to the new private purpose trust fund successor agency.

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Adjustments 10 and 11 also related to the dissolution of former OCDA and successor agency as of June 30, 2012.

The last adjustment related to OC Waste & Recycling stand alone financial statements.

Mr. Pulliam stated there may be additional findings related to the audit of the financial statements that would be added to the Single Audit Report before March 31, 2013. The finding provided more detail on the fifth adjustment for \$170 million. It was found during reconciliation and the matter was communicated to management and the financial statements were adjusted to reflect the change to be fairly stated.

Mr. Danley asked if the adjustments had any negative impact on the financials presented. Mr. Alfaro stated there were certain items in the bridge transfers and temporary transfers reflected and tracked on reconciliations. Such items were being aggregated or double counted in error in the cash and investments pool balance. Management was made aware and corrected the CAFR.

Mr. Pulliam stated that within the financial statements there were three main reporting groups: governmental activities (general funds and other governmental funds), business fund activities (such as JWA, OCWR) and fiduciary activities (such as investment trust fund). The adjustment pertained to the fiduciary funds of the County specifically the investment trust fund. While the adjustment resulted in an overstatement of net assets in the investment trust fund, it did not have an impact on the governmental activities or the business type activities of the County.

Mr. Franz asked the Treasurer and Chief Deputy Auditor-Controller if the misstatement had other impact as a result of the adjustment. Ms. Freidenrich stated she was not aware of any impact. She stated when the program initially started she understood the activities would be cross years. The temporary transfers were required by government code for the Treasurer to provide to school districts. When the program was set in place, communication began with Treasurer, Auditor-Controller's office and the external auditors and conceptually the program was in place. She explained how temporary transfers (fiduciary fund) were made to school districts and how the transactions were done. When money was loaned to the school districts, money also needed to be re-deposited into accounts and that transaction would need to be removed from the financials under the new process and it's where the adjustment occurred. Ms. Freidenrich stated they've reviewed the entries closely and was comfortable with the transactions going forward. Mr. Pulliam stated the program was also adapted to their risk assessment and audit plan and was where the adjustment was discovered in the reconciliation.

Dr. Carlson asked if the amount of the adjustment was a concern. Supervisor Nelson stated the amount was significant but because no money was lost it was not a concern. Mr. Pulliam stated the finding was classified as a significant deficiency.

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5. **Discuss and approve Director of Internal Audit request to contract with an external firm to conduct a Peer Review of Internal Audit Department for the three Fiscal Years ending 06/30/13**

Motion-Bates, Second-Nelson, Yes-Grimes, Yes-Franz, Yes-B. Hughes, Yes-Wille, Yes-Freidenrich, Yes-Carlson, Excused-Anderson

Approved as Recommended.

Directive: Dr. Hughes to provide back-up information of selected external auditing firm to Ms. Freidenrich.

Dr. Hughes explained the review cycle of the Peer Review. The professional standards require a review every third year. Internal Audit has had four reviews performed over the last 12 years. The reviews performed on Internal Audit were to validate the department's compliance with the following three standards organizations: the Institute of Internal Auditors (IIA), the American Institute of Certified Public Accountants (AICPA) and the U.S. Government Accountability Office (GAO). In the past, the Internal Audit Department relied upon an exchange of services with the California Counties Audit Chief's Association (CCACC) for the review to be performed. Dr. Hughes stated the Internal Audit Department doesn't have the available staff resources to provide services for a Peer Review at this time. He is requesting to hire an external auditor to perform the next Peer Review of IAD. The cost would be a not-to-exceed amount of \$14,000. The AOC is charged with the responsibility of selecting the Peer Reviewer to ensure independence. Dr. Hughes stated the external auditors are the same firm IAD used 10 years ago.

Ms. Freidenrich asked Dr. Hughes if there was any back-up to review and if he obtained bids from several firms for comparison. Dr. Hughes said IAD did research in the past to determine various vendors and related fees and stated Jefferson Wells was the preferred vendor used in the past. He said there were other mid-sized accounting firms and during one three-year period ended 12/31/2003 review cycle a different firm (Thompson, Cobb, Bazilio & Associates, PC, Washington, DC) was retained for the Peer Review that cost over \$60,000. Dr. Hughes stated the review would start in end of summer for Fiscal Year ending June 30, 2013.

Mr. Wille asked about the external auditor's experience. Dr. Hughes stated they were a general service provider and performed audits and were a national firm. Mr. Wille said \$14,000 was a bargain and the pricing was quite reasonable. Dr. Hughes stated he would provide a package of information to the AOC regarding the firm and stated IAD had a high level of confidence with the firm.

Supervisor Bates moved the item and asked Dr. Hughes to provide Ms. Freidenrich the back-up information on the firm and anyone else that requested it. The motion was seconded by Supervisor Nelson and the item carried.

6. **Receive the AOC Vendor Evaluation Subcommittee review results of the independent auditing firms for All Funds Audit solicitation and select primary and alternate to be presented to Board of Supervisors for approval to negotiate a contract. Provide direction to staff as needed.**

Motion-Nelson, Second-Bates, Yes-Grimes, Yes-Franz, Yes-B. Hughes, Yes-Wille, Yes-Freidenrich, Yes-Carlson, Excused-Anderson

Approved selection of Macias, Gini, O'Connell LLP as primary and Vavrinek, Trine, Day LLP as alternate for All Funds Audit to be presented to the Board of Supervisors at a future date for final approval to negotiate a contract.

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Ms. Grimes stated that at the AOC meeting in December 2012 a subcommittee consisting of Dr. Dave Carlson, Ms. Sally Anderson and Ms. Grimes was formed for the purpose of reviewing and scoring proposals for auditing services. The subcommittee met and received bids from two companies. The attachment provided the scores and prices. Both bids were responsive and competitive in pricing. The evaluation subcommittee recommended Macias, Gini, O'Connell, LLP based on scores. She stated the scores were extremely close between the two firms.

7. **Approve OC Internal Audit Department FY12-13 2nd Quarter Status Report for the period July 1, 2012 through December 31, 2012 and approve 2nd Quarter Executive Summary of Audit Finding Summaries for the period October 1, 2012 through December 31, 2012.**

Motion-Carlson, Second-Nelson, Yes-Grimes, Yes-Bates, Yes-B. Hughes, Yes-Wille, Yes-Freidenrich, Yes-Franz, Excused-Anderson

Approved as Recommended

Dr. Hughes stated the status report focused on the progression of accomplishing the audit plan. Dr. Hughes explained the follow-up audit process as well. Dr. Hughes described the audit universe and the audit categories. He said the status report detailed the audits completed and those in progress. Dr. Hughes explained the executive summaries were highlights of audits issued in the quarter.

8. **Approve 1st Quarter FY 12/13 External Audit Activity Quarterly Status Report for the quarter ended December 31, 2012**

Motion-Franz, Second-Nelson, Yes-Grimes, Yes-Bates, Yes-B. Hughes, Yes-Wille, Yes-Freidenrich, Yes-Carlson, Excused-Anderson

Approved as Recommended

9. **Receive and file Summary Highlights of Audit Reports Issued by Month for July 1, 2012 to January 31, 2013**

Motion-Franz, Second-Nelson, Yes-Grimes, Yes-Bates, Yes-B. Hughes, Yes-Wille, Yes-Freidenrich, Yes-Carlson, Excused-Anderson

Approved as Recommended

Dr. Hughes explained follow-up audits were performed six months following the issue of an original report. If corrective action was not implemented at that time, another six months is granted to allow for corrective action. If a finding was ranked critical, the auditee is required to implement intermediary corrective action or mitigate exposure immediately at a minimum.

10. **Nominate and appoint Chairman and Vice-Chairman for 2013 Audit Oversight Committee**

Appointed Supervisor Nelson as 2013 AOC Chairman and David Carlson as 2013 Vice-Chairman

Motion-Carlson, Second-Franz, Yes-Grimes, Yes-Bates, Yes-B. Hughes, Yes-Wille, Yes-Freidenrich, Yes-Nelson, Excused-Anderson

Dr. Carlson nominated Supervisor Nelson to serve as Chairman of the Audit Oversight Committee for 2013. Supervisor Nelson accepted.

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*Motion-Nelson, Second-Grimes, Yes-Franz, Yes-Bates, Yes-B. Hughes, Yes-Wille,
Yes-Freidenrich, Yes-Carlson, Excused-Anderson*

Supervisor Nelson nominated Dr. Dave Carlson to serve as Vice-Chairman of the Audit
Oversight Committee for 2013. Dr. Carlson accepted.

PUBLIC COMMENTS: None

AOC COMMENTS: None

ADJOURNMENT: 1:58 P.M.

NEXT MEETING: May 22, 2013, 1:30 p.m. REGULAR MEETING