

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, March 25, 2009, 1:00 p.m.

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

TELECONFERENCE LOCATION: IHS, Inc.
15 Inverness Way E
Englewood, Colorado 80112

Supervisor Patricia Bates
Member

Supervisor Janet Nguyen
Member

David Sundstrom
Chairman

Thomas G. Mauk
Member

Dr. David Carlson
Vice Chairman
Public Member

Chriss Street
Ex-Officio Member (non-voting)

ATTENDANCE: Patricia Bates, Janet Nguyen, David Sundstrom, Chriss Street, Tom Mauk, Bob Franz (Proxy), Dr. David Carlson

EXCUSED: Tom Mauk

PRESENT: County Internal Auditor, Internal Audit Department: Dr. Peter Hughes
County Counsel: Ann Fletcher
Clerk: Renee Aragon

1:00 P.M.

1. Roll Call:

Internal Audit Department: Peter Hughes, Eli Littner, Mike Goodwin, Autumn McKinney, Alan Marcum, Camille Gackstetter, Michael Dean, Renee Aragon; Auditor-Controller and staff: David Sundstrom, Claire Moynihan, Nancy Ishida, Christine Young, Ila Patel, Shawn Skelly; First District Supervisor: Janet Nguyen, Andrew Do; Fifth District Supervisor: Patricia Bates, Don Hughes; Treasurer-Tax Collector and staff: Chriss Street, Paul Gorman; County Executive Office: Tom Mauk, Bob Franz (Proxy received for Tom Mauk), Tom Beckett; County Counsel Office: Ann Fletcher; Public Member: Dr. Dave Carlson; Grand Jury Members: Gloria Wildman, Don Halpman, Terry Fleskes; Vavrinek, Trine, Day & Co.: Roger Alfaro, David Shoewalker Kevin Pulliam

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

2. Approve Audit Oversight Committee Minutes of December 11, 2009
VOTE: Motion-Bates, Second-Franz (proxy for Mauk), Sundstrom-Yes, Carlson-Yes
Nguyen-Excused
Approved

3. Receive Required Communications pursuant to SAS 114 from External Auditors, Vavrinek, Trine, Day (VTD) and Co.
No reportable action taken.

Mr. Kevin Pulliam addressed the Committee members and discussed the letter presented as required of VTD by AICPA's Statement on Auditing Standards 114. The letter addresses the Comprehensive Annual Financial Report (CAFR), the OC Development Agency, John Wayne Airport and OC Waste & Recycling. The letter documented VTD responsibilities and the County's responsibilities, audit scope, significant estimates and significant audit findings that included 4 new GASB standards that were implemented within the County's financial statements.

Supervisor Nguyen joined the meeting at 1:10 pm. Supervisor Nguyen asked for clarification on Page 6, Capital Improvements, Criminal Justice Facilities, Buildings and Improvements, Internal Service Fund. Mr. Roger Alfaro, VTD, stated the items make reference to accounting entries that were proposed as part of the audit. The first item, expense classification on the account balance and the second item represented a separate transaction from a different fund.

Mr. Street asked for clarification on page 6, Defined Benefit Plan, Benefit paid investment with trustee to reconcile OCERS trust of \$4m. Mr. Alfaro stated the entry pertains to the investment balance as reported in the financials at year end. As part of testing, there was one additional entry reconciled to the investment balance. On page 7, John Wayne Airport \$10m, Mr. Street asked if it was a credit. Mr. Alfaro stated the entry was a credit and represented a valuation of a complex at the airport. On page 8, Government Activities, \$70m entry for expenses and various functions, Mr. Street requested clarification because he felt it was a high dollar amount. Mr. Alfaro stated that when the financial statements were converted at year end from the fund level and during that conversion, this was one additional entry that resulted in expenses and income being grossed up and the entry was to reduce that.

This was in relation to the new accounting pronouncement. Dr. Carlson stated he agreed that the dollar amounts seemed rather large and requested additional explanation.

Mr. Alfaro explained the County made a payment during the credit year to set up and fund the OPEB obligation. In that process, on one basis of the county it was reflected as an expense and on the full accrual (or normal) of the county in the process, that entry/expense was converted to an asset. In that conversion process the expense remained in the income statement and the balance was adjusted in income to net it out. It was essentially reducing that affect to leave the net result of the asset on the County's financial statements.

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

Mr. Street asked if we were funding OPEB at that level of \$70 per year. Mr. Tom Beckett stated the amount reflected the initial funding of the trust at OCERS. He explained there was a transfer from County funds to OCERS in the initial balance in the county books a forehand and was transferred to OCERS. Mr. Street asked the approximate annual cost and was informed it would be less than half the amount.

Dr. Carlson had additional questions about the amount of adjustments on Schedule B. Mr. Alfaro stated the activity was not unusual because of the volume of detail. Typically exceptions would be found throughout the audit process.

Mr. Sundstrom stated he didn't recall why the note receivable of \$16m was recorded. Ms. Moynihan explained OC Public Works, Katella Yard sale was to occur in 06-07 and all proceeds should have received in 07-08 and the transaction should have been reflected in the books, but it was not recorded.

The item was a year-end accrual that was missed.

Dr. Carlson asked for clarity if any of the other entries were missed by management in the close of the books. Mr. Sundstrom responded yes.

Ms. Moynihan noted the items listed were all missed by management except for the \$70m because of how the money was allocated. The large dollar did not have a large affect on the financial statements. The others were due to being missed and there were a few changes to accounting theory approach related to debt. Mr. Sundstrom stated the parking lot at JWA was not missed, but was the result of discussions and some disagreements. Dr. Carlson stated he felt the issue was resolved by the external auditor and not internally. Dr. Carlson asked and stated that Schedule B was NOT cause for alarm or concern. Mr. Alfaro stated it was a fair statement. He added the management letter had not been presented to the AOC yet. He felt the management letter would provide some discussion about the issue and process. He felt none of the items presented caused them to rise to the level of significant deficiency in the financial statements. He stated that some of the items will be raised in the management letter findings but that the items even though large in dollar terms still did not rise to the level of a reportable significant deficiency.

Supervisor Bates asked that the County address some controls going forward to ensure that these types of adjustments wouldn't have these large numbers in the future. Mr. Sundstrom answered yes that they had been looking at what was in the management letter. Supervisor Bates noted that this was important information and that it should be sent to the Board in a memo. Mr. Sundstrom responded he would provide the memo. Ms. Moynihan added that the claims process would perform additional controls after the fact to ensure that the accounts payable accruals that should have been done at year-end were indeed done. If items are detected, adjustments would be done at that time. Mr. Sundstrom stated there would probably always be some level of adjustment but hopefully not as much in the future.

Mr. Mauk entered at 1:21 p.m.

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

4. Receive Status of the SIVs Held in the County's Investment Pool and related 2007/2008 CAFR Draft Footnotes and direct staff (continued from AOC 9/17/08, Item 6, 5/29/08, Item 5, 2/28/08, Items 6 and 8, December 11, 2009, Item 3)
No reportable action taken.

Mr. Paul Gorman provided a hand out and a status of the SIVs. He stated the balance continued to decrease with maturities and coupon payments. There remained one asset that went into receivership. The holdings of CCUSA matured. The K2 final holding would mature on June 9, 2009. Tango Finance final holding would mature on June 10, 2009. Whistle Jacket Capitol holding remained at \$62 million after an \$18m principal pay down last October. The Receivers announced they signed and memorialized the agreements with Goldman Sachs to go forward with a restructuring. It meant they would sell the assets in a competitive auction with a number of bidders and it was expected to occur on April 29, 2009. The location was uncertain. The Receiver stated they make some presentations and the County would have access to those to gain an understanding of what options would be available. Mr. Gorman stated as information was received it would be sent to the Board. Mr. Mauk asked what the value of Whistle Jacket on the books. Mr. Gorman responded \$84 million and stated our portfolio was still highly rated in spite of the downgrades.

5. Discuss Audit Oversight Committee Activity Calendar
No reportable action taken.

Dr. Peter Hughes presented the AOC Activity Calendar as a year-at-a-glance aide. It was designed for the AOC members and the public to identify the reoccurring events of the Audit Oversight Committee by quarter. It is considered a Best Practice in the profession. Dr. Hughes welcomed comments from the AOC regarding its content and utility. It was recognized as a helpful aid and supportive comments were made by AOC members.

6. Consider revising AOC Bylaws for AOC membership changes (continued from AOC 12/11/08, Item 4)
VOTE: Mauk-Moved, Nguyen-Second, Bates-Yes, Sundstrom-Yes, Carlson-Yes
The item was tabled.

Mr. Sundstrom stated he was considering changing the AOC Bylaws. He stated the background was that the preceding Grand Jury had recommended membership changes in a past report entitled "*Going, Going, Gone. Post Bankruptcy Controls.*" In the report, the Grand Jury recommended adding a member representing the Department of Education and a member representing the League of Cities. The concept was discussed at the last AOC meeting and at that time, Mr. Sundstrom recommended removing the Chair and Vice Chair of the Board of Supervisors from the AOC and instead adding public, non-County employees to represent each supervisorial district instead of the BOS Member themselves. Supervisor Moorlach at that time stated, the Board was evaluating the sizes of all the Boards, Commissions and Committees and requested the item should be continued for future discussion.

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

Returning this item to the agenda for discussion, Mr. Sundstrom stated he felt the Committee operated well and had been operating well for the past 10 years but felt at the margin it could get better if the Committee was represented by each Supervisorial District similar to the structure of PFAC. PFAC held five public committee members represented by each supervisorial district. Mr. Sundstrom noted that the AOC was the Board's committee and that unless there was 100% concurrence of the Board of Supervisors in making this change, he was not interested in recommending the change.

Mr. Mauk clarified that two membership compositions were being considered. First, the Grand Jury recommendation to add representatives of the school board and of the League of Cities; and second, Mr. Sundstrom's recommendation to add representatives from each supervisorial district replacing the Members of the Board themselves on the Committee. Mr. Sundstrom stated it was one solution to two questions. Mr. Mauk stated he did not support the second recommendation. He felt having the Board presence on the AOC was valuable and should not be removed. Mr. Mauk felt the AOC was different from the Treasury Oversight Committee and the logic to consider schools and league of cities was not needed at that time. Mr. Street stated there were two members of the school board on the Treasury Oversight Committee (TOC) appropriately. Mr. Mauk felt the scope of the work of AOC was mostly internal. Mr. Sundstrom stated he provided copies of his reports to the TOC and if they felt it important to attend the AOC meetings, they were open meetings and could attend at will; however, he did not see the benefit of adding school board members. Mr. Mauk moved to table the item and Supervisor Nguyen seconded.

Mr. Mauk left the meeting at 1:50 pm.

7. Receive and file Fraud Hotline Activity Report for the period July 1, 2008 through December 31, 2008

VOTE: Bates-Moved, Carlson-Second, Nguyen-Yes, Franz (proxy for Mauk)-Yes, Sundstrom-Yes

Received and Filed.

Dr. Hughes presented the Fraud Hotline Activity Report for the period of July 1, 2008 through December 31, 2008. He stated it was a best practice of the industry to make periodic reports to the Audit Oversight Committee regarding the hotline activity. Dr. Hughes reported there was an increase of 62% in activity from the prior reporting period. It was not an alarming number as the calls/complaints increased from 39 to 63 from the last reporting period. He stated the vast majority of calls come in during operating hours. He informed the Committee members that the hotline was monitored 24 hours a day and coverage was provided after hours by a contractor. Dr. Hughes explained the process and accessibility availability to employees, the public and vendors. He stated whenever an audit is conducted the auditee is informed that IAD oversees the County's Hotline and informs them how to access it.

Supervisor Nguyen requested an explanation about the purpose of the Hotline. She was concerned that the hotline was not being used for its intended purpose. She stated the callers should be referred to more appropriate departments to handle the issues and save staff and contractor resources and costs.

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

Dr. Hughes stated approximately half the calls received were referred out such as welfare fraud. IAD only addressed allegations under its sphere of influence. Dr. Hughes reported the cost for the contractor during off hours was approximately \$6,000 per year. He added IAD promoted availability to vendors, as well as to County employees, to report any suspicious behavior of other vendors or county workers. The coverage for the Hotline is broad and includes allegations of waste, fraud and abuse for county activities. He added that providing the 24 hour coverage was requested by the Audit Oversight Committee in the past so if employees were intimidated to place calls during working hours, the 24 hour access was provided for such instances.

Supervisor Nguyen requested a log of calls and activities to reevaluate and justify the need for a contractor to provide 24 hour coverage. Mr. Sundstrom stated it could only take one very bad call that might not have happened to place an incredible blemish on the County. It was that one call or that one possibility that he felt should keep the availability during nights and weekends. If there were zero calls, Mr. Sundstrom stated he would not recommend removing or canceling the hotline.

Mr. Sundstrom felt that a one-stop shop for a single County hotline should be considered. Supervisor Bates commented that Supervisor Moorlach raised a similar issue for OCTA and that because of confidentiality it was noted each individual agency should have its own hotline. Dr. Hughes stated that he does coordinate with other agency hotlines and that the unique and specialized nature of the DA's, HCA, and SSA programs required them to maintain their own hotlines as noted by Supervisor Bates regarding OCTA. Dr. Hughes welcomed the opportunity to provide additional data as requested by Supervisor Nguyen and stated he would have more data for the next AOC meeting. He stated that the Hotline Report was for their benefit in overseeing both County ethics and compliance programs and he welcomed their insights as to ways to improve its usefulness to them. Dr. Carlson stated it was not a good time to remove the 24 hour 7 day-a-week Hotline coverage given the current economic struggles. Supervisor Nguyen suggested renaming the hotline to the OC Hotline or to consider other name options that might have more appeal.

8. Approve OC Internal Audit Department Status Report for Period October 1, 2008 through December 31, 2008, and Executive Summaries of Audit Finding Summaries for the Period October 1, 2008 through December 31, 2008

Approved.

VOTE: Nguyen-Moved, Franz (proxy for Mauk)-Second, Bates-Yes, Sundstrom-Yes, Carlson-Yes

Dr. Hughes explained the status report and explained notations or comments. He stated that IAD had its budget cut by one administrator and two auditor positions that were vacant. Due to the budget reductions, IAD had to assign to audit management the full time duties of the administrative position. Dr. Hughes stated that nearly 1400 hours were removed from next years audit plan as a result. With those changes, he noted that the IAD was on schedule to complete its planned audits, subject to the approved revisions. Dr. Carlson asked why the payroll audit on page 4 was delayed. Dr. Hughes noted that while the sheriff payroll was on the audit plan, the BOS directed the Performance Audit Director to look at their overtime issues at about the same time IAD was planning to start the audit. Therefore, IAD postponed the audit to allow the Performance Audit Director to complete their audit.

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

The IAD would still pursue the payroll audit because it had the highest payroll of any department; and they were also the only department not part of the VTI electronic time recording system. The audit would be started within one month. Mr. Street and Mr. Sundstrom stated they were in discussions with Sheriff staff about joining VTI. Mr. Sundstrom commented about the CAPS+ implementation and shared services work. He offered purchasing services to IAD if needed. Dr. Hughes responded it was a great offer but didn't expect any activity because there was no money to spend. Mr. Street stated Mr. Sundstrom was considering consolidating the collections office with the Treasurer's office and felt there would be a great benefit. He stated it was a concept only and that many issues need to be addressed with the unions.

Dr. Hughes discussed IAD participation in the CAPS+ implementation in assessing the adequacy of internal controls in the systems. It had been a very successful participation. The status of all audit findings in the follow up audit process was presented. Dr. Hughes was pleased to report that the majority of all recommendations were implemented by the first follow up.

9. Receive and file External Audit Coverage 2nd Quarter Status Report FY 08/09

Received and filed.

VOTE: Carlson-Moved, Nguyen-Second, Bates-Yes, Franz (proxy for Mauk)-Yes, Sundstrom-Yes

Dr. Hughes stated a summary was provided and the audits were tracked until resolution. Dr. Hughes stated some items held a long shelf life. There was no material issues brought to the attention of the AOC this past quarter. Supervisor Bates stated the BOS discussed a review of a contractor's service delivery in Social Services Agency and felt it would possibly be an area Internal Audit could assist. She noted that the CEO office began the review but the information would be needed in an urgent matter. Supervisor Bates would speak with the CEO and get back to Dr. Hughes. Dr. Hughes stated certainly that Internal Audit would rally resources for any item the BOS or AOC felt urgent.

10. Nominate and appoint Chair and Vice-Chair for 2009 Audit Oversight Committee and approve 2009 AOC meeting dates.

Nominated and appointed David Sundstrom as Chairman of the Audit Oversight Committee for 2009 and nominated and appointed David Carlson as Vice-Chairman of the Audit Oversight Committee for 2009.

VOTE: Bates-Motioned, Sundstrom-Second, Nguyen-Yes, Franz (proxy for Mauk)-Yes, Carlson-Yes

Supervisor Bates nominated David Sundstrom as Chairman and David Sundstrom nominated David Carlson as Vice Chairman of the Audit Oversight Committee for 2009. The motion was seconded by Dr. Carlson and the item carried.

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

Public Comments – *At this time members of the public may address the AOC on any matter not on the agenda but within the jurisdiction of the AOC. The AOC may limit the length of time each individual may have to address the Committee.*

No comments.

AOC COMMENTS & ADJOURNMENT:

AOC COMMENTS: none.

ADJOURNED: The meeting adjourned at 2:25 p.m.

NEXT MEETING:

May 27, 2009, 1:00 p.m., Regular Meeting