

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, September 21, 2011, 10:00 a.m.

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

Supervisor Bill Campbell
Member

Supervisor John Moorlach
Member

David E. Sundstrom
Vice-Chairman

Thomas G. Mauk
Chair

Dr. David Carlson
Public Member

Shari Freidenrich
Ex-Officio Member (non-voting)

Steve Danley
Ex-Officio Member (non-voting)

ATTENDANCE: David Sundstrom, Bob Franz (proxy for Tom Mauk), John Moorlach, Bill Campbell, Shari Freidenrich, Steve Danley, David Carlson – observed by teleconference

EXCUSED: None

PRESENT: Director of Internal Audit
County Counsel:
Clerk:

Dr. Peter Hughes, CPA
Ann Fletcher
Renee Aragon

10:00 A.M.

1. Roll Call

Internal Audit staff – Mike Goodwin, Autumn McKinney, Alan Marcum, Eli Littner;
Auditor-Controller Staff – Nancy Ishida, Dat Thomas, Claire Moynihan; Second District Staff – Lindsay Brennan; Fourth District Staff – David Zenger; External Auditors Vavrinek, Trine & Day – Kevin Pulliam, Roger Alfaro, David Showalter

Dr. Carlson observed the meeting by teleconference. Posting requirements per the Brown Act were not available to his location and he was unable to cast votes on the item. His participation was recorded as excused for each vote.

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

2. Approve Audit Oversight Committee regular meeting minutes of April 27, 2011
Moved-Sundstrom, Second-Franz, Yes-Moorlach, Yes-Campbell, Excused-Carlson
Approved as Recommended, with revisions

3. Receive SAS 114 Required Communication from External Auditors Vavrinek, Trine, Day and Company, LLP
Moved-Franz (proxy for Mauk), Second-Sundstrom, Yes-Campbell, Yes-Moorlach, Excused-Carlson
Approved as Recommended

Mr. Kevin Pulliam addressed the AOC as required by the standards SAS 114. The audit scope, timing and field work were discussed. VTD is responsible to express an opinion on whether the County's financial statements as prepared by management with the oversight of the Board were presented fairly in all material respects and conformity with generally accepted accounting principles. VTD is required to provide reasonable but not absolute assurance about the financial statements on whether they were free of material misstatements. VTD considers internal controls but no opinion would be expressed on internal control. Controls over financial statements and OMB compliance requirements that could have direct and material impact over each of the major federal programs of federal funding and federal expenditures the County receives. VTD does however express an opinion on compliance when it is applicable to federal programs including the passenger facility charge report from John Wayne Airport and the redevelopment guidelines of the redevelopment agency. VTD noted the State came out with a new audit guide for redevelopment agencies (RDA) and new compliance requirement. Because of the new compliance guide, there will be new audit standards as they related to redevelopment agencies. Mr. Pulliam stated additional communication will be provided to the AOC as the audit progresses of the items mentioned. VTD conducts the audit from a risk based audit approach. The risk assessment was an ongoing process throughout the audit. The key business cycles were documented and the design for operating the effectiveness of the majority of the internal control systems. Planning for the Single Audit and major programs had begun. For each of the reporting segments of the audit, an exit communication would be provided to the AOC.

Mr. John Moorlach stated the external auditors, on the unfunded pension liability, used the entire amount of OCERs as opposed to stating only the Orange County portion. He felt it was an overstatement in the disclosures of what Orange County's unfunded liability actually was and hoped the County could assist VTD to gain a more precise number from OCERs for disclosure. Mr. Pulliam stated the County was currently gathering data for the CAFR process and they would meet with the staff responsible for preparing the footnotes and pose the question for disclosure. Ms. Shari Freidenrich, as a member of the OCERs Board, agreed to provide assistance if possible. Mr. Sundstrom stated he instructed the CAFR team to segregate out the costs that were specific to the County. GASB required interim reporting in the footnotes, but didn't limit further disclosure as appropriate. He stated they had received information from the CFO on liabilities. Mr. Sundstrom shared his concern and was moving in the same direction. Mr. Moorlach stated he reviewed the footnotes on the pension liabilities and retiree medical and there was not an amount stated for retiree medical that he could find and requested clarification.

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

Mr. Moorlach asked Mr. Sundstrom, as relates to GASB, if Orange County could get ahead and show unfunded liabilities on the balance sheets now as opposed to later when it became affective. Or, if able, to provide a supplementary schedule at the back of the basic financial statements that detailed liabilities and provide financial statements with those reflected liabilities. Mr. Sundstrom stated, as GASB was proposing now, it would be effect fiscal years ending June 30, 2013 for Orange County because of the size. Earlier implementation would be encouraged with every pronouncement GASB released. However, he understood it would required a phenomenal amount of work for OCERs for all plan sponsors and a total rework of the actuarial detail that OCERs would need to provide. Orange County would rely upon OCERs actuary data as required. He anticipated information would be available 2012 that would require a presentation for 2013. Mr. Sundstrom said some objections were received at GASB and 12 major constituent groups sought a 60 day delay, but won't be allowed. They may possibly grant a 15 day maximum. He stated GASB expected to be on target for fiscal year starting June 2012.

Ms. Freidenrich stated the OCERs Board received a presentation from David Sundstrom on GASB impacts at its strategic planning meeting. She stated OCERs, if plan sponsors requested certain services; those services could be charged against their income so that it wouldn't affect the others. Ms. Freidenrich stated she would discuss with the OCERS Board to provide more specifics. She said a contributing issue for OCERs was that it has a December 31 year end and participants followed a fiscal year calendar. Mr. Moorlach clarified that GASB sought the valuations as of June 30 as opposed to December 31 information. Mr. Sundstrom agreed. Mr. Moorlach noted CalPERS would need to get ahead. Mr. Sundstrom stated 18 month data in arrears could be used with certain roll forward procedures for actuary assessment. Mr. Moorlach noted an unrecognized gain or loss for the reporting period. Mr. Sundstrom said census information would be used as of December 31 and then project the benefits based on the census. It would not be a full evaluation. He said a full evaluation would be to provide a new census on all plan members and use that data for projections.

Mr. Moorlach asked if a different interest rate assumption would be used if the plan was not funded at a certain level. Mr. Sundstrom stated that issue was expected to be controversial and debated by GASB and presented at the public hearings upcoming in New York, Chicago and San Francisco. He said AICPA, GFOA and one other organization were expected to testify in New York. Mr. Sundstrom stated he felt the cash flow methodology of using prorata 70/30 and allow an assumed rate of return at 70 and using a bond rate for the remaining 30 was complex. He felt the bond rate was not related to cash flow analysis and the maximum rate on the remaining 30 should be the rate of inflation because nothing was set aside for liability. He felt it should be discounted back because it was projected forward. Mr. Sundstrom said the present value of liability should be discounted back with the interest on what was hoped to be earn with what was gained and the inflation rate based on wasn't realized, but his colleagues on GASB didn't necessarily agree.

Mr. Moolach said the NET assets that were dedicated to capitol assets less liability related to those and restricted by outside parties and NET unrestricted. Mr. Sundstrom said that if in a liability stance, the unrestricted is the bottom line and it would be wiped out. Mr. Moorlach asked how OC would reflect in the year that we implement the major adjustment. He asked if the prior year financial statements would be restated or an extra-ordinary number reported.

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

Mr. Sundstrom said that issue was not deliberated yet. He said that implementation would be deliberated as we go forward. Since we are presenting comparative years in the first year, he would guess it would be a restatement of the first year so it wouldn't necessarily affect the operating statement of that implementation, but the matter was yet to be discussed and decided.

Mr. Moorlach asked the external auditors if \$3.7 billion for pension was used and \$400 million for medical, the adjustment would be \$4 billion to the Orange County CAFR and noted it was material. It is a dramatic statement. Mr. Pulliam stated it was that way for all governments. Mr. Moorlach asked a non specific question that if the City of Laguna Niguel and outsourced to OCFA for fire services and OCSD for public safety services the proportion of UAL reflected on OC books and not on the City books. Mr. Moorlach asked if the disclosures could state that clarity. Mr. Sundstrom suggested to isolate the operating costs from pension contributions and have the contract city make a commitment to pay it separately in the language of the contract. Mr. Moorlach requested for Bob Franz to address the issue when the contracts are presented to the Board in June 2012.

Mr. Sundstrom stated, while on pension and CAFR, he was concerned that OCERS did not plan on issuing their CAFR from last year until November 2011 and how that would affect Orange County for attestation work and delivery of opinion on the OC CAFR. Mr. Pulliam stated they would need to evaluate the information provided from OCER included in their CAFR or as Required Supplementary Information (RSI) related data and how it flowed through certain components. Mr. Pulliam stated the RSI was referenced in the report and there was a disclaimer associated with the RSI however they do not opine on the RSI. The RSI needed to be consistent. Mr. Franz asked if the external auditors would issue the OC report in December and how the OCER CAFR would affect OC. Mr. Alfaro stated they need to wait until they receive the information.

Ms. Freidenrich confirmed OCERS is delayed to issuing their financials. Some of it related to OPED benefits disclosure and how it was handled. The OCERS auditors Macias, Gini were seeking additional information before they opine on their reports. She will ask if there is information that can be released to assist OC with their statement before it is published. Mr. Pulliam stated they will work with CAFR implementation team. Mr. Franz stated several dates that OCERS CAFR had projected for completion were all extended and suggested the County make plans in the event they will not be released in November. He said the preliminary information was that findings of material deficiencies were expected and additional questions about qualified or unqualified were not answered. Mr. Franz stated the OCERS external auditors were expected to declare material deficiencies in the audit and possibly lead to qualified opinion. Ms. Freidenrich said the new OCERS auditors hold a different opinion from the prior auditor over certain trust funds and disclosure. Mr. Sundstrom asked if one of the major causes of the delay was from a understaffing of the new auditors. Ms. Freidenrich stated they were busy and OCERS audit staff were assisting them. Mr. Sundstrom stated OCERS hired a highly qualified internal auditor with 3 certifications. He was a past president of Beach Cities Chapter of IIA and was employed by the City of Los Angeles. Mr. Franz stated the assistant CEO in OCERS was hired as well, Ms. Brenda Shott formerly of OCTA.

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

4. Approve OC Internal Audit Department 4th Quarter Status Report of FY 10-11 for the period July 1, 2010 through June 30, 2011, and approve 4th Quarter Executive Summary of Audit Finding Summaries for the period July 1, 2010 through June 30, 2011
Moved- Moorlach, Seconded–Franz (proxy for Mauk), Yes-Sundstrom, Yes-Campbell, Excused-Carlson

Approved as Recommended

Dr. Peter Hughes stated the report detailed the full year of audits and projects completed. Notes reflect activity for item as required. It covered a variety of financial, internal control, information technology, revenue generating leases, and the hotline activity. Mr. Steve Danley suggested coordination over the ICE audit because Performance Audit was performing a correction medical follow up and some aspects may overlap. Mr. Moorlach stated he met with the assessor and discussed effective use of technology and expected a report that he would like Internal Audit to review. He referenced footnote 4, and asked if IA was tracking billable hours. Mr. Moorlach asked how when audit issues surface that Internal Audit to alerted the Board. Dr. Hughes stated when timely or immediate issue surface, Internal Audit instituted an Audit Alert Report to alert the Board and management timely.

5. Approve External Audit Coverage 4th Quarter Status Report FY 10/11 for the period July 1, 2010 through June 30, 2011.
Moved-Moorlach, Second-Franz (proxy for Mauk), Yes-Sundstrom, Yes-Campbell, Excused-Carlson

Approved as Recommended

Dr. Hughes stated there were no material issues to relay for the reporting period. He stated at any point of time about 100 external audits occurring throughout the county. Some related to grants or state programs. Mr. Moorlach asked if the JWA opening, vendors would pay a development fee for the (page 9 of 20), who could OC contact regarding FAA regulations and wants JWA to pay for fees and we get a return on investment/cost on construction. Dr. Hughes stated Eli could research information and get back to him.

PUBLIC COMMENTS: NONE

AOC COMMENTS: Mr. Danley stated Performance Audit Department was doing an audit of risk management (enterprise risk management).

ADJOURNMENT: 11:04 A.M.

NEXT MEETING: December 7, 2011, REGULAR MEETING