

COUNTY OF ORANGE
AUDIT OVERSIGHT COMMITTEE

MEETING MINUTES
Wednesday, September 24, 2003, 2:00 p.m.

The Audit Oversight Committee of the County of Orange met on September 24, 2003 at 2:00 p.m., in the Hall of Administration, Building, 5th Floor, Conference Room B, Santa Ana, California.

Members Present/Absence Noted:

Present: Mr. James Ruth, Interim CEO
Mr. David Sundstrom, Auditor-Controller
Dr. Dave Carlson, Public Member
Absent: Supervisor Tom Wilson, Chair Board of Supervisors
Supervisor Jim Silva, Vice-Chair, Board of Supervisors
Mr. John Moorlach, Treasurer-Tax Collector, Ex-Officio Member

1. Call to Order: (David Sundstrom, Chairman, Audit Oversight Committee)

Mr. Sundstrom called to order the meeting on July 23, 2003 at 2:03 p.m. Mr. Sundstrom asked for roll call before proceeding with the agenda.

Committee Members:

Mr. Ruth, Mr. Sundstrom, Dr. Carlson

Guests:

Internal Audit Staff: Dr. Peter Hughes, Eli Littner, Michael Goodwin, Autumn McKinney, Alan Marcum, Renee Aragon, Auditor-Controller Staff: John Nakane, Claire Moynihan, Macias, Gini and Company: Jean Horimoto and James Godsey, HCA Staff: Jeff Nagle, Julie Poulson, Dave Riley

2. Approval of Minutes from July 23, 2003 (David Sundstrom, Chairman, Audit Oversight Committee)

Recommended Action: Approve

Approved as recommended.

3. HCA Office of Compliance Presentation (David Riley, HCA/Compliance Officer)

Recommended Action: Discussion Only

Julie Poulson, Director of Health Care Agency addressed the committee and introduced Mr. David Riley, Compliance Officer. Mr. Riley addressed the committee and reported that HCA Office of Compliance (HCA OC) started three years ago and was created to ensure compliance with health care industry standards and strict federal and state guidelines. Mr. Riley introduced Dr. Nagle and stated that he was the Operational Officer for HCA OC. Dr. Nagle was a member of the National Health Care Compliance Association and also an officer in Region IX and had become an expert in compliance. Dr. Nagle addressed the committee and presented a power point hand out and gave an overview of the elements within the program.

Dr. Nagle reported that the HCA OC program had quickly become an industry leader and guided state level technical and training assistance when requested. He explained the key objective to the compliance program was to create a process for identifying and reducing risk and improving internal controls. The essence of the program was to find those areas that were potential liabilities to the agency and then put in place either monitoring or training. They put external audits on high risk areas or self audits on other key areas. Dr. Nagle stated hotline calls average approximately 80 per year and approximately 15 were substantiated. He stated training was key to a compliance program and its effectiveness. The next steps identified in the program would allow for changes in regulations and remain effective. Mr. Ruth asked about employee receptivity. Dr. Nagle stated employees were starting to rely less on the hotline and focus and confide more with management and communication. The Committee Members complimented them all for a successful program and pledge support for their continued endeavors.

4. Macias, Gini and Company – Required Communications
Recommended Action: Discussion Only

Mr. Godsey addressed the committee and explained the required communications. He stated governmental audit standards require that the external auditors meet and communicate with the Audit Oversight Committee each year and go over the scope of the annual audit engagement. Mr. Godsey reported that on May 29, 2003, MGC signed a new contract to continue working with Orange County. He stated they are extremely please to be reselected and given the opportunity to continue working with the County. He explained the audit would be of the financial statements prepared in compliance with GASB34 reporting model. He stated that last year the County had done exceedingly well and had a great start on the new reporting model. Mr. Godsey stated the disclosures to allow for easier reference uses of the management letter. Additionally the CAFR, single audit coverage, separate opinions on internal controls and compliance would be done. As part of their contract, they would also issue stand-alone financial statements on JWA, IWMD, Development Agency and the County Special Finance Authority. In addition to the opinion, they would also be doing a report on internal controls for the entity as a whole and a separate report on internal controls in compliance over the federal programs. The reporting responsibility for the external auditors provides for reasonable and not absolute assurance of the financial statements.

5. Sarbanes-Oxley Act of 2003 (Dr. Peter Hughes, Director, Internal Audit Department)
Recommended Action: Discussion Only

Dr. Hughes explained the intent and coverage of Sarbanes-Okley Act (S/O Act). Dr. Hughes noted that the County of Orange had for the most part embraced and implemented many of the S/O Act requirements years ago. The S/O Act also required the establishment of a hotline program and periodic reporting to the committee regarding the nature and composition of the hotline activity. Dr. Hughes reported that Internal Audit had an establish hotline program and reported the activity annually for the last eight years. He stated that the reporting activity would be added to the quarterly status reports for more frequent reporting to the AOC. He stated the HCA program and partnership with Internal Audit was very productive and he was pleased with the on-going progress. Mr. Marcum, Audit Manager, passed out the most recent report on Internal Audit hotline activity and explained the hotline investigation process.

Mr. Sundstrom asked how internal audit was promoting the availability of the hotline to county employees. Dr. Hughes reported that when Internal Audit presents Control Self-Assessment reviews, they bring to the attention of the participants the availability of the internal audit hotline program. Mr. Marcum added that the department webpage would also provide information about the program. Dr. Hughes stated more thought would be given to the distribution of poster advertisement.

6. Status Report #3 – Period 01-01-03 to 9-23-03 (Dr. Peter Hughes, Director, Internal Audit Department)

Recommended Action: Receive and File

Approved as recommended.

Dr. Hughes stated that he would focus the status report presentation on certain audit categories on a quarterly basis. Ms. McKinney was introduced as the Audit Manager overseeing Information Technology Audits. Ms. McKinney stated the team consisted of one senior auditor and one extra-help position. She noted that all IAD auditors and audit managers took the CISA and the majority passed. She stated the extra help position was helping implement the monthly Computer Assisted Audit Techniques (CAAT) reviews. Internal training was being done to allow for the release of the extra-help position. Ms. McKinney reported that in addition to the CAATs, two IT reviews had been done this year – the Auditor-Controller Check Writing and the IWMD/LIST implementation.

She handed out an IT self-assessment questionnaire developed by the team for County departments' use and stated it was based on the COBIT framework. She stated it had been given out to all departments. Additionally as part of the annual audit risk assessment, Internal Audit was trying to compile an inventory of all key systems in the County. She stated the team had been requested to share the information and inventory with CEO/IT. Ms. McKinney reported on internal training for auditors and department plans on rotating audit staff through IT reviews to build coverage and experience. Mr. Marcum added that during other reviews the auditors could also gain systems understanding and the benefits of that understanding reveal themselves in identifying possible systems risk or control weaknesses. Ms. McKinney reported another tool, SYSTRust, was being evaluated as an audit approach to provide assurance of the effectiveness of controls over the availability, security, integrity and maintainability of the systems. Dr. Hughes stated Internal Audit planned continued communication with CEO/IT.

Mr. Sundstrom applauded the efforts of Internal Audit in its IT audit coverage and continued development. Ms. McKinney stated CAP 34 would be revised by the end of the year for the review of the Auditor-Controller.

7. External Audit Activity Fourth Quarter FY 02/03 Status Report (Dr. Peter Hughes, Director, Internal Audit Department)

Recommended Action: Receive and File

Approved as recommended.

Dr. Hughes gave a brief description of experience of the auditor assigned to monitoring external audit activity. Dr. Hughes stated Mr. Dan Melton's accumulated experience brought great benefit to the monitored coverage.

8. Executive Summaries of Audit Assignments, Period 4/3/03-7/23/03 (Dr. Peter Hughes, Director, Internal Audit Department)

Recommended Action: Receive and File

Approved as recommended.

Dr. Hughes explained the follow-up process and coverage. He stated that the AICPA was giving this topic great attention. Mr. Marcum gave a brief summary of the reviews in the Treasurer's Office.

Dr. Hughes noted page 3, Attestation Services & Mandates, Audit of Treasury Investment Compliance for Two Years Ending December 31, 2002, Internal Control and Compliance Issues Noted, specifically no. 1. He sought the direction and assistance of the AOC because Internal Audit reached a professional difference of opinion with the Treasurer. When revisions were reviewed, Internal Audit noted that original language dictated by a Board directive to be included in the IPS was changed by the Treasurer Tax Collector (TTX). The TTX stated it was changed for clarification. Internal Audit feels the language change changed intent. It was believed by Internal Audit that the change allowed for the purchase of investments that had split ratings. The Treasurer does not believe that the changed language changed the intent.

Mr. Sundstrom asked about the IPS approval of the Treasury Oversight Committee (TOC) prior to Board approval of the changes. Mr. Sundstrom added that the TOC found inadvertent changes in the IPS that was never approved that had slipped in. Mr. Sundstrom asked if a word-by-word comparison was done. Mr. Marcum explained that software was used to compare the various revised IPS's and showed exactly what words were changed. Based on those changes identified, Internal Audit validated if the TOC was informed of the changes and if the BOS was informed and approved the changes. Mr. Sundstrom asked if the language was approved by the TOC. Mr. Marcum stated yes that a letter from the Treasurer to the TOC dated October 10, 2001 explained that change was needed because the language was confusing. The clarification given to the Board of Supervisors on the change was a wording simplification. Mr. Marcum stated in the proposed IPS for 2003, dated December 3, 2002, the wording in the December 18, 2001 IPS was completely eliminated. The eliminated wording was not noted in the proposed IPS dated November 1, 2002 given to TOC members at the November 6, 2002 meeting. In addition, the eliminated wording was not identified as a revision in the cover letter dated December 3, 2002 for the Board to review and approve.

Specific attention was brought to the IPS, page 6, item 1A, the disagreement was with interpretation of the changed language. The March 27, 2001, IPS stated, "No security purchase may have a rating of any of the three nationally recognized rating agencies of less than the minimum rating required for that class of security." The December 18, 2001, IPS stated, "No security at the time of purchase may be rated below the minimum required under this policy." Mr. Marcum reported the body of the Policy dated December 18, 2001 stated there must be two ratings that meet the requirement. Therefore the difference was changes from three ratings to two ratings. Dr. Hughes stated the Board directive was clear to not allow for split rated purchases. Internal Audit believed the language changed the directive and intent of the Board. Dr. Hughes noted that the Treasurer believed that he was still prohibited from buying split rated purchases. Internal Audit professionally disagreed with the Treasurer's conclusion, which was why this issue was brought before the Committee Members in accordance with AOC policy.

Dr. Hughes recommended that the AOC direct an expert or specialist to evaluate the differences and resolve the interpretation. Dr. Hughes said another option would be to reinstate the original language of the Board directive reflected in the March 27, 2001 IPS. Dr. Hughes noted that the Treasurer stated he made the changes to allow for consistency and phraseology.

Mr. Sundstrom stated that he and public member, Dr. Carlson, would speak with Mr. Moorlach to seek clarification of intent to changes of IPS. Mr. Sundstrom said he was on record at the TOC as disagreeing with the language change. Mr. Sundstrom said the next TOC meeting would address this audit and he would move a motion for re-approval. The issue would be brought to attention there.

9. Next Meeting

◆ December 3, 2003, 3 p.m.

Agenda Item Suggestions/Action

Mr. Sundstrom requested the Risk Assessment Summary and proposed audit coverage status if available.

10. Public Comments

None

11. Adjournment

The meeting was adjourned at 3:50 p.m.