

**Independent Mendocino County Audit Committee
August 11, 2010**

An Independent Mendocino County Audit Committee should be established. This Committee would be a permanent body with significant authority to conduct the annual audit of the County's financial statements and perform other duties. It would also be charged to conduct a broad investigation of problems with the County and Retirement Association's financial management and propose solutions.

Such Audit Committees are a normal function among private for-profit and non-profit organizations. These recommendations are based on many of the well-known concepts of such Committees.

In addition, these recommendations are highly informed by similar recommendations made in the "Kroll Report" regarding the City of San Diego and other government-related information sources. The Executive Summary of the Kroll Report provides a good context of the need of such a Committee in the context of local government.

Independent Mendocino County Audit Committee

1) Permanent Independent Audit Committee

A Mendocino County Audit Committee similar in concept to the common practice in private sector organizations should be organized.

a) Mission

To assure the public and County officials that the County of Mendocino's financial reports are truthful and meaningful, that the County's financial planning and control systems perform at a high level, and that the public has the financial information necessary to truly hold County officials accountable.

b) Organization and Structure

The Audit Committee shall have five members.

i) Public Members

Three "public" members shall be County residents who have no identified conflicts of interest regarding the County and are not employees or agents of the County or any directly related organization. They shall possess the independence, experience and technical expertise to carry out the duties of the Audit Committee. This expertise includes but is not limited to knowledge of accounting, auditing and financial reporting. The minimum professional standards for public members shall include at least 10 years of experience as a certified public accountant or as a certified internal auditor, or 10 years of other professional related financial or legal experience." One of these public members shall be selected by the full Audit Committee to Chair the Committee.

The process of selecting the public members must assure the County's private professional financial community that the public members are highly capable, truly independent, and committed to the principles of the Audit Committee.

ii) Member of Board of Supervisors

The Board of Supervisors would have a permanent standing Finance and Planning Committee. One of its County Supervisor members would be on the Audit Committee. This Supervisor will have no additional authority on the Audit Committee.

iii) County Employee

Three current "regular" employees of the County shall be nominated by all current regular County employees to be on the Audit Committee. These individuals must have at least 10 years of significant financial work experience and be familiar with auditing, financial reporting and analysis. The three public members shall select one of these three nominees to be on the Audit Committee.

c) Oath

All members of the Audit Committee, including the County Supervisor, will sign an oath that the fundamental duty of the Committee is to the citizens of Mendocino County, and that they will use their expertise to the best of their ability to make sure

- i) the County's financial reports provide a truthful and understandable picture of the County's finances, conform to generally accepted accounting principles and legal requirements, and provide good information for County decision makers.
- ii) the County's financial management meets the following general duties:
 - Tell the important truths about the County's finances.
 - Manage the County's finances competently and transparently.
 - Build and preserve the County's financial strength.
 - Don't force unfair costs onto future County residents and taxpayers.
- iii) The County has an effective program to prevent fraud, waste and abuse.

d) Independence

The Audit Committee would operate with complete independence from the County Board of Supervisors, the Chief Executive, the Auditor-Controller and Treasurer-Tax Collector, the Retirement Board and Administration, and all other individuals and bodies in County government and MCERA. The method of selecting outside members of the Audit Committee needs to produce members who will be seen by most of the County's private-sector financial professionals as both capable and truly independent.

e) Control Over Annual Audit and Outside CPA

The Audit Committee will hire and direct the outside CPA in the production of the County's annual audited financial statements. It would have authority to hire and direct other outside advisors and clerical support. It would have authority to inquire into and report regarding all aspects of the County's finances, including planning, control and reporting.

The Board of Supervisors will direct all County employees and agents to cooperate with the Audit committee and to provide the Committee with requested materials.

f) Other Functions and Powers

The Committee shall have the authority and responsibility to -

- Monitor County official's expense accounts and use of County assets,
- Receive and evaluate complaints received from any source regarding the County's accounting, internal controls, financial planning and reporting, maintain the confidentiality of the sources of those complaints, and monitor their resolution.
- The Committee shall review and report on the quality of the "internal audit" functions in the County and the reports of those functions.

g) Committee Budget

The Board of Supervisors would provide a budget adequate to perform these functions. The outside members of the Audit Committee should receive a reasonable fee for their time; to do this function probably will take some significant time. If a member of the Audit committee has staff available (for example was a CPA in practice locally) the Audit Committee could provide a reasonable reimbursement for clerical support provided by that Committee member's staff.

h) Committee Reports

The Committee will produce at least two annual reports in addition to the CPA's audit report. The first Committee report will be addressed to the Board of Supervisors. This will identify how the Committee discharged its duties, significant accounting - internal control - and compliance issues, discuss the review of the financial statements - annual reports - accounting issues, and discuss the auditor's report.

The second report will be addressed to the residents of the County. This will provide a general analysis of how well the County's financial management fulfills the duties defined above. It will generally describe the County's general financial condition and identify significant financial strengths and weaknesses.

i) Related Organizations

The Audit Committee will identify organizations within the boundaries of Mendocino County:

- Which have potentially significant impact on the finances of the County of Mendocino.
- In which County officials have significant (not necessarily majority or dominant) impact on the selection of or control over their governing bodies and/or executives.

These organizations will include but not necessarily be limited to:

- Mendocino County Employees Retirement Association
- Mendocino County Air Quality Management District
- Mendocino County Public Facilities Corporation
- Mendocino County Water Agency
- Mendocino County Library District
- Redevelopment Agency of Mendocino County
- IHSS Public Authority Governing Board

The Audit Committee will determine the extent to which the finances of these organizations including the impact of these organizations on the finances of the County should be integrated into the Audit Report from the outside CPA and/or the Audit Committee's reports.

If separate audit reports are or must be produced for any of these organizations that are controlled by the Board of Supervisors or other County officials then they are included within the scope and authority of the Audit Committee as defined herein.

If separate audit reports are produced for any of these organizations that are not controlled by the Board of Supervisors or other County officials the Audit Committee will review and analyze those reports and the finances of those organizations and include the Committee's findings and recommendations in its reported defined

j) Timing

If possible this should be implemented for the 2010-2011 audited financial statements. But it should be implemented no later than the end of calendar year 2011 and should be fully functioning for the 2011-2012 audit.

2) Initial Independent Audit Committee Investigation and Report

The Audit Committee in its first year would conduct an investigation into a broad range of issues related to the County's debt and the financial management of both the County and Retirement Association and produce a report of its findings and recommendations. The goal would be to produce such a report no later than the end of calendar year 2011, but preferably by the end of the June 2011 fiscal year.. This report could include recommendations to pursue further investigations and analysis.

The Board of Supervisors will provide funds necessary to conduct this Investigation and Report. These funds will be in addition to those provided to accomplish the Committee's duties defined in "**Permanent Independent Audit Committee**" above. The Committee will have the same powers and independence as defined in that previous section.

The general goals of this investigation and report are two-fold:

a) Identify What Has Happened

The Audit Committee Report should "get to the bottom" of all significant issues regarding the County's debt and financial obligations, the County's and Retirement Association's financial management (including financial planning, accounting, financial reporting, internal controls, etc.), and possible instances in which significant legal requirements were not complied with.

In addition to retiree benefit-related County debt and obligations, other issues would include the "Teeter Debt", the operation of the County's "investment pool", the Mental Health Fund (including its financial relationship with the State of California), and all other similar potentially significant sources of County financial obligations or flaws in the County's financial management.

This investigation would also include issues internal to the Retirement Association. Included in such issues would be a reconstruction of financial flows within the Association's funds including the Pension Fund and Funds for the payment of Retiree Healthcare since and including 1998. It would include identification and analysis of all methods used to calculate Pension Fund "Excess Earnings" and an evaluation of whether or not the methods used complied with legal requirements.

Also included would be a review of the County's and Retirement Association's compliance with Government Accounting Standards Board and other financial control, accounting and reporting requirements.

The scope of this investigation and report is not limited to the range of issues normally thought to be that of a financial audit. The scope encompasses all significant aspects of financial management. Included are the adequacy of funding for retiree benefits, the appropriateness of the use and management of the County's various funds and financial "pools", controls for capital assets (inventories of County automobiles, etc.).

The scope is limited to financial management; it does not extend to "general policy" issues. For example, a specific topic to be addressed in the Report would relate to the County's retiree benefits. The Audit Committee will not make recommendations regarding what those benefits should be. The Committee will report about how the County's benefits should have been properly funded, what would be required in the Committee's opinion to properly fund them in the future, and how the real expenses and obligations of these benefits should be reported to the people.

b) Proposals to Accomplish Financial Management Goals

The Committee Report would include proposals that would assure the residents of Mendocino County that County officials will be held accountable to fulfill the financial duties defined in "**Permanent Independent Audit Committee**" above.

Included would be topics such as the County's planning systems (especially the incorporation of long-term financial planning on a full accrual financial model), internal controls, methods to specifically assign responsibility and accountability for important aspects of the County's financial management (such as the accuracy of financial statements, the complete disclosure of all material financial risks, etc.), the format and information contained in the financial statements of both the County and Retirement Association, and other similar material topics.

References

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