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## OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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**Date Issued:** November 15, 2007

**IBA Report Number:** 07-112

**Audit Committee Date:** November 19, 2007

**Item Number:** 4

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# Professional Audit Consultant Update & Suggestions for Consultant Reports

## OVERVIEW

At the meeting of the Audit Committee on October 15, 2007, the IBA discussed a proposal by Jefferson Wells (the audit consulting firm selected by the Audit Committee) to change one of the two lead consultants to the City due to an unanticipated change in personnel. The Committee supported the IBA's recommendation for a meeting with the Jefferson Wells team, including the new lead consultant, to discuss Committee expectations before executing the consultant agreement. This report provides a brief update on that meeting, and further recommends specific consultant tasks and deliverables for the Audit Committee to consider requesting.

## FISCAL/POLICY DISCUSSION

### Meeting with the Jefferson Wells Team

The IBA arranged for a meeting with Chairman Faulconer and the Jefferson Wells team on October 5, 2007. Jefferson Wells was represented by Debbi Frazier (Managing Director for the Southern California Region) and the two lead consultants, Ron Steinkamp (Director, Internal Audit and Controls) and Jim Santer (Internal Controls Consultant). Chairman Faulconer discussed Audit Committee expectations regarding consultant availability, audit related issues and expressed a desire to further enhance the effectiveness of the Committee. The Jefferson Wells team reiterated their interest and commitment to meet the needs of the City's Audit Committee.

Following the meeting, the IBA and Councilmember Faulconer agreed that the Jefferson Wells consulting team was well qualified and motivated to provide needed audit expertise to the Audit Committee. The decision was made to execute an agreement with Jefferson Wells. Given the need for the Jefferson Wells consultants to occasionally interact with the City's Internal Auditor or other City staff, a meeting was held on November 8, 2007 to introduce the Jefferson Wells team to the City's new Internal Auditor Eduardo Luna and COO Jay Goldstone. It was agreed that Jefferson Wells role was to add value to the City's audit related processes and that all would strive for cooperative interaction.

### Recommended Initial Scope of Work

In addition to being available for expert advice at each meeting of the Audit Committee, the IBA suggests that Jefferson Wells be assigned several tasks and associated deliverables to present to the Committee over the next several months. Drawing from the broader scope of work possibilities outlined in previous IBA reports and the City's Audit Consultant RFP, we have developed a draft scope of work with associated deliverables for the Audit Committee to consider (see Attachment). Summarizing from the attachment, the following six tasks/reports were developed to provide expert analysis and best practice recommendations for issues related to the work of the Audit Committee:

- Present a written report to the Audit Committee describing best practices associated with development of an annual audit work plan.
- Present a written report to the Audit Committee summarizing the City's identified internal control issues/deficiencies and provide best practice remediation suggestions. Rank identified internal control deficiencies in terms of perceived risk and importance.
- Present a written report to the Audit Committee evaluating effective public audit programs. Provide short-term, intermediate and long-term suggestions for optimally staffing/funding the City's audit organization.
- Before the City's FY 06 financial statements are presented for Audit Committee consideration, present a written report evaluating the current Audit Committee process for reviewing the City's annual financial statements. Comment on best practices from other comparable public agencies and on the information provided by the Ad-Hoc Advisory Committee.
- Present a written report to the Audit Committee describing critical processes and attributes for an effective internal employee hotline. Provide short-term and long-term recommendations for complying with the Kroll recommendation for City Auditor and Audit Committee involvement.
- Identify useful training that could be reasonably provided to members of the Audit Committee. Provide training for the City Council on important standards and regulations related to the role of the legislative body in reviewing/approving public financial statements.

## CONCLUSION

The professional audit consultant contract with Jefferson Wells has been executed. Lead consultants Ron Steinkamp and Jim Santer will be present for the Audit Committee meeting on November 19, 2007 and at all meetings in FY 08 thereafter. In addition to their standby ability to address audit related items that may arise or stem from Committee meetings, the IBA recommends the Committee request that Jefferson Wells research and report on specified matters of interest to the Audit Committee.

The IBA has attached six possible tasks and associated deliverables for the Audit Committee to consider in this regard. As there are only one or two Audit Committee meetings remaining in calendar year 2007, one possibility would be to request that the audit consultants present one report each month to the Audit Committee beginning in January 2008. As stated in previous reports, the IBA believes that the professional audit consultants will be valuable resource for the Audit Committee and the City Council. We recommend that the consulting team be immediately utilized as needed and be provided with special research direction at this meeting.

**[SIGNED]**

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Jeff Kavar  
Fiscal & Policy Analyst

Attachment

**[SIGNED]**

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APPROVED: Andrea Tevlin  
Independent Budget Analyst

**Audit Committee: Professional Audit Consultant  
Suggestions for Consultant Assignments in FY 08**

**Task #1:** Listen to the presentation updating the Audit Committee on the status of the citywide risk assessment on November 19, 2007. Discuss those processes that are underway for assessing organizational risk, and the planned approach for developing an annual audit work plan, with the City's new Internal Auditor.

**Deliverable:** Present a written report to the Audit Committee describing best practices associated with development of an annual audit work plan. Discuss how effective public audit committees are typically involved with the development of an annual audit work plan. Provide suggestions as to how effective public audit committees are apprised of audit work plan developments and outcomes during the fiscal year. Recommend processes for receiving audit reports and following up on auditor recommendations. How can the Audit Committee best ensure that audit recommendations are implemented and effective? Comment on your understanding of the annual audit work plan development process being undertaken by the City's Internal Auditor.

**Task #2:** Review the City's 2005 and 2006 Report on Internal Controls. Also review the "Yellow Book and Single Audit Report" prepared by Macias Gini & O'Connell as part of their audit of the City's FY 05 financial statements. Discuss efforts to improve the City's internal controls with the City's Chief Operating Officer, Internal Auditor, Comptroller, and the Chief Information Officer to better understand the work in progress.

**Deliverable:** Present a written report to the Audit Committee summarizing internal control issues and deficiencies that have been identified in the above reports. Rank the identified internal control deficiencies in terms of perceived risk and importance. Discuss the City's remediation efforts to date and/or planned remediation efforts. Comment on the City's planned utilization of a new ERP system to address certain internal control issues. Drawing from best practices and/or organizational expertise, make suggestions that could help the Audit Committee or City staff to better address identified internal control issues. If there is a particular role for the Audit Committee to perform in evaluating or following up on an internal control issue, specify what that role should be.

**Task #3:** Evaluate the City's need to develop an effective annual audit program. Research staff and budget allocations at comparably sized public agencies with effective audit programs. Consider staff and any related resources that might be needed.

**Deliverable:** Present a written report to the Audit Committee with your analysis and findings. Provide short-term, intermediate and long-term suggestions for optimally staffing the City's audit organization. Describe different performance metrics for judging the effectiveness of an audit organization. The Audit Committee and the City Council will be considering this information in their review and adoption of the City's FY 09 budget.

**Task #4:** Observe and evaluate the current Audit Committee and City Council process for reviewing the City's FY 05 financial statements. Research recommended best practices and effective programs at other public agencies for legislative review of financial statements. Discuss the City's financial statement review process with the Audit Committee's Ad-Hoc Advisory Committee, and review their recommendations. Review the best legislative practices for retaining an outside auditor and reviewing the annual audit of public financial statements.

**Deliverable:** Present a written report to the Audit Committee describing your findings before the FY 06 financial statements are presented for consideration. Provide the Audit Committee with a sense of how the City's current review process compares with those of other comparable public agencies. Make suggestions as to how the City might improve its review process. Suggest ways to best facilitate Audit Committee communication with the City's outside auditor.

**Task #5:** The Kroll Report recommended the new Audit Committee have responsibility for the establishment and monitoring of effective policies and procedures for dealing with “whistleblower” complaints, including an internal hotline. Kroll further recommends a process whereby the Audit Committee receives a report for each complaint and, in consultation with the City Auditor, determines the appropriate course of action. Review hotline recommendations from the Kroll Report and research how effective employee hotlines are utilized by other public agencies. Review the current Employee Hotline being administered by the Mayor’s Office of Ethics & Integrity.

**Deliverable:** Present a written report to the Audit Committee describing critical processes and attributes for an effective internal employee hotline. Describe successful hotlines being utilized by other comparable public agencies. Understanding current staff resource limitations and that the recommendation for a City Auditor reporting to the Audit Committee requires voter support in June 2008, recommend how the Audit Committee might best comply with the Kroll recommendation prior to the June election. Assuming that voters approve the recommendation for an independent City Auditor, recommend a process for the Audit Committee, and the City Auditor to more fully comply with the Kroll recommendation. Discuss necessary resources associated with the above recommendations.

- Task #6:**
- 1) Identify specific training that could be reasonably provided to members of the Audit Committee to better prepare them for their legislative oversight responsibilities.
  - 2) Provide training for the City Council on important standards and regulations (as set forth by GASB, GAAS, SAS, etc.) that relate to the role of the legislative body in reviewing/approving public financial statements.