

Chair Report and Recommendations

Agenda Item: Consideration of CBOC position on District refusal in providing requested resources-Initiation of Performance Audit Process.

Date: October 11, 2012

Summary This report focuses on the Annual Performance Audit and how this effort can address one of our significant resource requirements identified earlier i.e. a “select forensic” audit. The report analysis and recommendations move us towards the preparation of an Annual Performance Audit. The Audit would address many of the process, protocol, procedure, and compliance questions among others that are part of the Independent Oversight function of our committee.

The remaining legal and independent financial requirements have been rejected by the Superintendent remain outstanding. The Committee may wish to discuss and ask staff for advice whether a discussion on this issue is appropriate for a Closed Session Item. By bring up this question, the Chair is making the argument for the necessity for an “as needed” independent legal firm. For instance, there may be other such questions relating to the Brown Act.

Recommendations

1. Hear specific comments, suggestions, and areas of concern from the Committee and members of the Public on the Audit Scope.
2. Request that an Audit Committee Finalize a Scope of Work with District Staff for a thorough Performance Audit as outlined in the Government Auditing Standards issued by the Comptroller General of the United States.
3. Direct the Performance Audit include a thorough and exhaustive analyses of least three mutually agreed upon problematic projects for the Proposition O Bond Program within the last three years.
4. Discuss what additional actions, if any, should occur to the Districts no funding letter regarding legal, audit and independent financial consultants.
5. Authorize the Chair to make any corrections to any factual issues or typos/grammatical mistakes in this agenda item and noted as part of the official public record.

Background

There have been the following actions related to this agenda item:

On August 16, 2012 our Committee approved a letter to the Board of Trustees on a number of issues. This included a recommendation for an independent financial consultant, legal resources, and a select forensic audit.

This letter was presented to the Board of Trustees on August 20, 2012. Subsequently on August 25, 2012 the Superintendent verbally indicated this funding would not be forthcoming.

On September 6, 2012 a letter drafted by the Chair was presented at our Bond Oversight Committee Meeting responding to the funding recommendation from the Superintendent. After the drafting of the letter and prior to the Committee meeting the Chair received a letter from Dr. Brand stating that the funding request was denied.

The Committee directed that the September 6, 2012 letter be revised, reviewed by a Subcommittee, and forwarded to the Trustees.

After the September 6, 2012 Committee meeting, the Chair met with the Executive Director of the California League of Bond Oversight Committees to discuss the forensic audit. He felt that our forensic audit could be incorporated in the Annual Performance Audit and funded by bond proceeds not the General Fund. The Chair suspended further drafting of the response letter given this advice by Calboc.

Performance Audit

As indicated above, one of the major components of our requested services/resources from the District was what was termed a “select forensic audit.” The text in italics below is provided from the letter received earlier by our Committee:

The specific scope of work could include the following:

- *Review of Financial and Performance Audits to Date*
- *Conduct interviews of facilities and accounting personnel to gain an understanding of the Districts procurement process, internal controls over Proposition “O” Funds and other possible areas of concern*
- *Obtain general ledgers for the Proposition “O” Funds for select periods and perform financial analyses to identify total funding received, total expenditures incurred, and identify major projects*
- *Compare actual project expenditures to approved budgets to identify cost overruns*

We believe the Forensic Audit should review select problematic projects during the tenure of Seville and post Seville to determine what occurred during each period and what, if any, changes were made by the District.

As indicated above, The District responded that they cannot provide any resources to complete any of the items requested including the “select forensic audit”. Also, at the September 9, 2012 meeting Member Morris mentioned to the need for more information regarding the revised scope and budget.

When the Chair met with the Executive Director of the California League of Bond Oversight Committees, there was considerable discussion back and forth regarding the scope and funding. The conclusion after the meeting and further discussions was the “select forensic audit” as described above could be incorporated into the annual performance audit required for review by bond oversight committees. The Performance Audit can be paid for out of bond proceeds pursuant to the California Education Code. Thus no District general fund costs would be required for funding. Most importantly what is termed the “Yellow Book” aka Comptroller General of the United States Government Auditing Standards provide the basis for the audit scope as described above.

The Executive Director of the California League of Bond Oversight Committees recommended the review of the recently completed Performance Audit for the West Contra Costa County Unified School District. The Chair reviewed the report, its costs, and discussed the study with the firm who completed the audit. Where appropriate relevant information has been included in this report.

The sections below will discuss this issue further. There is one very unfortunate reality we should have already started the process for retention of a consultant, as the statutory deadline for completion and certification is March 31, 2013. It is doable if we agree to start in motion the process tonight and work closely with staff to set deadlines and expectations early on.

The following sections questions and answers are provided as follows:

Why is a Performance Audit Required?

Proposition 39: The Safes Schools and Accountability Act that allowed for a 55% voter approval and number for other related measures contained language regarding Citizen Oversight. AB 1908 signed by the Governor and contingent on the successful passage of Proposition 39, set in motion the implementing measures for Independent Citizen Oversight.

AB 1908 requires an annual performance audit. It requires us to receive and review the Audit. **The ultimate control over the Audit Control, Scope and Funding is the Board of Trustees. Thus while the Committee has the basic**

charge to do a number of reviews of the Bond Program and the Performance Audit provides the tool do a lot this work, the ultimate authority to actually allow us to do this is beyond our legal control so far.

On September 6, 2011 SB 423 was signed by the Governor which required the annual, independent financial and performance audits must be conducted in accordance with the Government Auditing Standards issued by the Comptroller General of the United States for financial and performance audits and be completed by March 31, 2013.

What should be included in a Performance Audit?

There are no specific “cookie cutter” guidelines for a specific scope of work for a Performance Audit of a School Bond Program. However the Government Auditing Standards issued by the Comptroller General of the United States for financial and performance audits does contain significant guidance on the Scope of the Audit Work for an overall Performance Audit. The Government Auditing Standards Handbook reference above has two full chapters (Chapter 6: Field Work Standards for Performance Audits, Chapter 7: Reporting Standards for Performance) devoted to the topic. Both Chapters are found as an attachment to this report.

An example of the specific guidance with respect to a performance audit contained in Section 7.20 which deals with Internal Controls should serve as one example of the differences between Financial and Performance Audits. The referenced Section is entitled “Deficiencies in Internal Control”. The following is the text of the language: “

“In a performance audit, auditors may conclude that identified deficiencies in internal control that are significant within the context of the audit objectives are the cause of deficient performance of the program or operations being audited. In reporting this type of finding, the internal control deficiency would be described as the cause.”

Financial Audits usually focus almost exclusively on data/numbers and their validity, accuracy, reliability. As can be seen above, Performance Audits can deal with process and control issues and how well a program is being managed.

What is the relationship between the Performance Audit and the Statutory Mission of the Bond Oversight Committee?

Education Code Section 15278 (b) states the overall purpose of our Committee: “The purpose of the citizens' oversight committee shall be to inform the public concerning the expenditure of bond revenues. The citizens' oversight committee shall actively review and report on the proper expenditure of taxpayers' money for school construction”

The process and control processes for all elements of bond projects will ultimately impact the cost effectiveness and help us evaluate whether we have had a proper expenditure of funds. There are a host of potential elements that can be included in the Performance Audit for a School Bond Program (See below).

What was the major scope of work elements for the West Contra Costa County Performance Audit?

As indicated above, the California League of Bond Oversight Committee Executive Director felt that the scope of this District's Performance Audit was the most comprehensive and thorough of such recent such audits. Their scope items were as follows:

- Composite Bond Measures Final Report. The objective of this section was to report on the financial activities of the District's bond program. The objective included analyses of the District's compliance with bond language and legal limitations regarding the issuance of bonds under the terms of the various voter-approved measures and monitoring the bond proceeds after issuance regarding investments and arbitrage regulations. This scope item could, for instance, have called out any risky or problematic investments such as Capital Appreciation Bonds so prominent in the press lately.
- Compliance with Ballot Language. The objective of this section was to report on the financial activities of the District's bond program, including analyses of the District's compliance with bond language and legal limitations regarding the issuance of bonds under the terms of the voter-approved measure and monitoring the bond proceeds after issuance. This analysis made sure that actual project expenditures are in conformance with the stated ballot language. This component of the audit also includes an assessment of assessed value (AV) in relation to statutory limitations and how projected AV growth relates to forecasts of project needs.
- Compliance with State Law and Regulations. The objective of this section was to assess the overall compliance with some of the pertinent legal and regulatory requirements governing a school district facilities program. The District developed this assessment of compliance to analyze the functionality of the District's bond facilities program. It should not be viewed or relied upon as a legal opinion or a complete analysis of all state laws and regulations.
- Compliance with District Policies and Regulations. The objective of this section was to assess compliance with some of the pertinent District

policies and regulations governing the District's facilities program.

- District and Professional Services Staffing Plan for the Bond Program. The purpose of this section was to gain an understanding of the District's policies and approach to in house and consultant staffing for managing the measures and the effectiveness of the staffing related to the number of bond program projects.
- Program Management Effectiveness. The purpose of this section was to gain an understanding of the District's process of managing the measures programs and the effectiveness of the use of staff and consultants in the management and implementation of the planning, design and construction of the program projects.
- Design and Construction Schedules Cash Flow Analysis. The objective of this audit section was to review the methods utilized by the District and their consultants to track the schedule of available revenues and expenditures for all projects and to plan each building project in accordance with the availability of funds.
- Design and Construction Costs and Budgets. The objective of this section was to gain an understanding of the established District process for the development and adherence to design and construction budgets on bond funded projects in the facilities construction program; to gather and test data in order to determine compliance and measure the effectiveness of controls.
- Bidding and Procurement Procedures. The purpose of this section was to gather data and verify that District bidding and awarding of bond funded construction projects comply with the requirements of the Public Contracting Code, state and other relevant laws and regulations.
- Change Order Procedures. The purpose of this section is to gather data and review change order documents to verify that the processing of change orders for bond funded construction projects comply with the requirements of the Public Contract Code, state laws and other regulations.
- Claim Avoidance Procedures. In this section, there was an evaluation and review of the procedures used to limit the number of claims filed against the District related to construction projects.
- Expenditure and Payment Procedures. The objective of this performance audit section was to verify that the District was compliant with its policies and procedures related to Proposition 39 expenditures and payments. The scope of this performance audit section was to verify transactions of

funds expended during the fiscal year ended June 30, 2011.

- Best Practices in Procurement. The purpose of this section was to gather data and verify that District bidding and awarding of bond funded construction projects comply with the requirements of the Public Contracting Code, and other relevant laws and regulations and to ensure that best practices in procurement are followed.
- Delivered Quality Analysis. The purpose of this section is to evaluate the District's processes related to setting standards for products and systems to be included in the facilities projects, to ensure that the standards are incorporated into the design and documentation, and to ensure that the designed systems are included in the final construction of the project. An additional objective was to gather and test data in order to determine compliance and measure the effectiveness of controls.
- Monitoring Local Participation Requirements and other Related Board Policies. The purpose of this element was to determine compliance with specific Board Policies such as local business or Minority Women Owned Business Participation.
- Effectiveness of Bond Communication Program. The objective of this section was to determine the effectiveness of the District's communication of the Bond Program and progress to community members and stakeholders.
- Review of Bond Oversight Committee Meeting Minutes. The objective of this performance audit section is to validate that the Citizens' Bond Oversight Committee (CBOC) met as scheduled, that meeting minutes were appropriately taken, and that a quorum of members was present to approve the meeting minutes.
- Citizens Bond Oversight Committee Compliance. The objective of this performance audit section is to assess the overall compliance of the Citizens' Bond Oversight Committee (CBOC) with law, the District's Board Policies and the Committee's bylaws. This section, together with the section entitled "Review of Citizens' Bond Oversight Committee Meeting Minutes," provides a comprehensive assessment of CBOC issues.

Not all of these components are required for our Audit. However the scope items provide an example of the necessary elements we probably should seriously consider for inclusion in the type of audit we require as an Independent Oversight Committee.

What should is the estimated cost for such an Performance Audit?

This will ultimately depend on factors: 1) What is the policy decision by the Board on what they want to have audited with hopefully our concurrence on the contract scope? 2) What resources will be committed by the District and the Oversight Committee to assist the consultant? 3) Will the District organize data supplied to the consultant in such a manner that it can be easily understood i.e. will it require a lot of consultant time in “massaging” and clarifying the information?

There are some elements of the Contra Costa County Audit that may not be necessary to analyze (e.g. completeness of minutes). There may be other however that may need to be added. The cost of the West Contra County Audit was \$141,000.

Based upon the completeness of this audit (254 pages) and number of subject areas covered it should serve as a sound basis for our Audit rough estimate of costs at this time. My review of the Audit Scope appears to meet our overall requirements.

For discussion purposes and for inclusion in an RFP I would recommend at conservative round number through the possible exclusion of some scope items, that we have a maximum budget amount of \$125,000 to be subject to negotiation once we selected the most qualified consultant.

It is critical and good practice to only get to the issue of cost after we select the most qualified consultant who can objectively and without bias or interference provide the requested audit. As a benchmark to the estimated maximum cost, the last expanded Performance Audit with Eric Hall Associates cost \$65,000 (see Eric Hall Report 9).

Why do we need another expansive Audit if Eric Hall Associates did one less than a year ago?

Eric Hall did not complete some of the work elements mentioned above. For instance there was not a a “soup to nuts” analysis and review of problematic projects to determine what if any improvements, deficiencies, or actual best practices were utilized. Eric Hall was selected by a District Only Committee with the scope also dictated by the District.

This Performance Audit should be different. While the Board of Trustees must approve the Audit scope and funding, this Bond Oversight Committee should demand a direct involvement in the development of the Audit Scope, consultant selection, and feedback to the consultants during Audit preparation.

Is there any reason why the District should resist a detailed Performance Audit?

Not really, as there are millions of dollars at stake. There could be substantial

potential savings identified well in excess of actual audit costs through process improvements. Some of these process improvements could have spillover or implications for other District operations. For example, it could be a way for the District to know if the proposed staffing plan for the Bond Program is adequate to meet the demands.

A multi million dollar business should periodically have such a review as good business practice. Why not the District? If the District has initiated substantial improvements since the departure of the last Superintendent what better vehicle than an independent audit results to report to the taxpayers. Most importantly, we now have an engaged, active, and mindful Oversight Committee of its role. This Performance Audit is so important to use while completing our work.

What is a Proposed Schedule?

The schedule is tight, as we must have this completed by March 31, 2013. Using the prior schedule for last years Audit and my personal experience in my former life as a County of San Diego Project Manager, here is the recommended schedule:

- 10/11 CBOC Discussion and Input to Audit Committee
- 10/25 Request for Qualifications Solicited
- 11/7 RFQ Due
- 11/5-11/9 Evaluation/Interviews
- 11/12-11/16 Negotiation of Contract
- 11/19 Board Approval
- 2/15 First Draft
- 2/22 Second Draft
- 3/14 Submittal of Final Report/CBOC Approval
- 3/31 Project Completion
- April 2013 Board Discussion and Recommendations

For this schedule to be met, there are a number of concurrent, early start, or process initiatives that must be in place:

- There needs be an internal agreement on most if not all of project scope early on so that the District can begin basic data collection and organization now so the consultant, whoever it may be, can “hit the ground running” upon contract execution.
- Because the CBOC meets only once month, the Audit Committee must be empowered to give recommendations and suggestions to District Staff/Consultant during the process.
- An electronic accessible Proposition O data base should be developed now for those staff, consultants, and oversight committee members to be

available for the Audit to facilitate the communication within the consultant engagement.

- There should be single point of contact from the Committee to respond to immediate inquiries or troubleshooting.
- While we are getting organized in terms of scope and have a philosophical consensus on the general breadth of the audit, staff should move forward even before the RFQ issuance to put the consultant community on notice of our pending requirements and schedule. We must have an open and transparent solicitation process. Your Chair is committed to spend the necessary time that this open good business practice is in place.

I am sure there are other items we should start now. This is just an initial observation.

Contact: Nick Marinovich 619-934-4982 Email: nickmarinovich52@gmail.com