



STATE AUDIT COMMITTEE

MONDAY, DECEMBER 9, 2013, 10:00 A.M.
RHODES STATE OFFICE TOWER
30 EAST BROAD STREET, 35TH FLOOR, JUPITER/SATURN CONFERENCE ROOMS
COLUMBUS, OHIO 43215

Members Present: Paolo DeMaria
Beverly Vitaz
Kai Monahan
Ryan Hecht

Members Absent: John Merchant

Call to Order

Chairman DeMaria called the meeting to order at 10:00 a.m.

Approval of Minutes

Mr. Monahan moved for the minutes of the meeting held September 23, 2013 to be approved with no additions or corrections. Mr. Hecht seconded the motion and all members unanimously approved.

IT Optimization Update

Chairman DeMaria introduced Stu Davis, State Chief Information Officer from the Department of Administrative Services (DAS) to update the Committee on the state's IT Optimization process.

Mr. Davis mentioned that disaster recovery and security practices currently differ at state agencies and a consistent posture is needed. He believes that the quality of services will not be sacrificed with a centralized IT function and should improve it. The centralized function also creates employee development opportunities. He also stated that housing the State's IT assets in a central location results in cost savings and more focus on the business.

Mr. Davis mentioned some examples of their centralizing efforts which are in three focus areas – Ohio's Private Cloud, Enterprise IT Shared Solutions, and Online Services. He said that the Department of Transportation has agreed to process their transactions in OAKS, the State's information system. Ohio Business Gateway is also undergoing changes for entities to have a single registration when conducting business with the state. He also stated that the Department of Job and Family Services and Department of Youth Services will be the last two agencies to move to the state's email platform, planned to occur in January. Mr. Davis' team is also looking at requirements for agency geographic locations instead of each agency analyzing bandwidth on their own.

Mr. Monahan asked about the cost savings, and Mr. Davis stated that they estimate \$20 million in savings has occurred over the past 12 months and that \$100-165 million in savings would be realized in approximately five to seven years. The main challenge has been not impacting the business processes with the centralization effort. Mr. Monahan asked about the security in place for the cloud environment. Mr. Davis stated that there are two components which are based on federal requirements. He recommended that David Brown from DAS come to the next Audit Committee meeting to speak about security.

Chairman DeMaria asked if the agencies were getting used to the IT Optimization initiative. Mr. Davis said that the majority of the agencies are supportive, but this effort will take time and patience; sometimes they have to convince the agencies of the benefits. Mr. Davis admitted that DAS' customer service needs to improve. Mr. Bell stated that he appreciates Office of Internal Audit's (OIA) relationship with Mr. Davis and DAS' Office of Information Technology and that OIA has remained involved in the designing of the IT Optimization process. Mr. Bell mentioned the OIA projects that involve DAS, such as the SOCC remediation and Integrated Eligibility and that they are going well. Chairman DeMaria thanked Mr. Davis for his time.

Office of Budget and Management Audit Oversight Workgroup Update

Chairman DeMaria introduced Janet Conkey, Senior Deputy Director of Services and Operations at the Office of Budget and Management (OBM). Ms. Conkey discussed the Audit Oversight Workgroup in place at OBM to follow up on state agency management letter comments from the Auditor of State. Ms. Conkey mentioned that since her last update, the workgroup has included some new members and has more clearly defined the function of workgroup. The workgroup was created because Director Keen (OBM) realized that many of the Auditor of State management letter comments received by the state agencies were not being addressed and were repeated from audit to audit. Ms. Conkey also stated that having this workgroup helps OBM employees recognize agency strengths and weaknesses and match training resources across agencies for common issues.

Ms. Conkey talked about the members of the group and their backgrounds. The group meets monthly and reviews the most recently issued state agency management letters and related agency responses. The group rates the comments as low, moderate or high risk, and based on the agency response, determines if any follow up is needed. The OBM budget analyst for that particular agency is responsible for any follow up. Ms. Conkey stated that the workgroup has reviewed approximately 140 management letters. Of these, 20% had no comments, upon which OBM provided a written commendation to the agency. For the remaining 80%, there were 300 comments for which the workgroup has placed into eight primary categories. This helps OBM identify what type of assistance is needed at the agencies, such as best practices on depositing receipts or paying expenses, or areas of lesser risk such as disaster recovery or records retention. The workgroup is also working with the Auditor of State on how to address the comments on the lack of reconciliation with OAKS.

Ms. Conkey said that the next steps for the workgroup include the identification of trends and performing data analysis which will include uploading historical data and using the database for tracking remediation. This analysis will utilize automation and ease some of the administrative

burden on the workgroup members. OBM will also work on agency policy and create appropriate internal and external training.

Ms. Vitaz asked about the significance of the comments being reviewed. Ms. Conkey stated that Mr. Bell is helpful in assigning the risk level and helps to drive how they work with agencies. Mr. Bell pointed out that the workgroup only analyzes management comments, not yellow book comments, significant deficiencies or questioned costs. The management letter comments could be material to the agency.

Mr. Hecht stated that the database analytics were a positive step and asked if it should be limited to management letter comments only and whether other types of communications have been considered. Ms. Conkey stated that currently the communications have been limited to agency directors and internally with OBM. The subject matter areas have also been included in the Ohio Fiscal Academy curriculum. Mr. Hecht recommended including material weakness trends in their database as well. Mr. Bell pointed out that the Auditor of State includes material weakness trends in their single audit report and he agreed that communication is important for organizational improvement. Chairman DeMaria asked who was monitoring the more significant comments and Ms. Conkey stated that Jim Kennedy monitors the material single audit comments and a corrective action process was already in place. Chairman DeMaria thanked Ms. Conkey for her time.

OBM Financial Reporting Update

Jim Kennedy, Deputy Director of State Accounting and Reporting, and Amy Hall, Financial Reporting Manager, OBM, spoke about the CAFR preparation timeline. Mr. Kennedy stated that an aggressive schedule had been established for OBM Financial Reporting and the Auditor of State for completing the preparation and audit of the State's Comprehensive Annual Financial Report (CAFR). Both parties collaborated on the timeline. The audit of the CAFR has not been issued by the end of December since 2004.

A key date that has been met was the October 15 deadline for the college and university audits. OBM Financial Reporting provided draft financial statements to the Auditor of State by November 27. This was one and one half weeks sooner than the previous year. For the Auditor of State, their audit time was reduced by three weeks, which is quite aggressive. Mr. Kennedy considers this year's process to be a success and that there is a good chance to meet the goal. Mr. Kennedy mentioned that every year has challenges, such as new pronouncements and changes in reporting entity. Receiving the agency reporting packages on time was another key achievement. Chairman DeMaria asked if there were any significant changes for next year. Mr. Kennedy stated that the Ohio Turnpike Commission will be assessed as to whether it should be included in the reporting entity, as well as the issuance of debt for the Department of Transportation and pension reporting.

Mr. Kennedy also discussed the highlights of the FY 2013 State of Ohio CAFR. He provided a snapshot of some unaudited financial statement item comparisons. He mentioned that there were no significant accounting pronouncements for FY 2013. He spoke about the state's liquidity in that there was over \$5 billion in the General Fund at the year-end; OBM was able to

transfer almost \$1 billion in the State's Budget Stabilization Fund; and liquidity has improved compared to prior years. Regarding the change in the unrestricted portion of the state's primary government net assets, the negative amounts that have been reported are trending down, which corresponds to the decline of Unemployment Insurance debt with the federal government. Mr. Kennedy also mentioned that the negative amount in the Governmental Fund includes \$7.81 billion of debt issued for state assistance to component units and local governments, whereby those entities report the corresponding asset. Mr. Kennedy also stated that OBM is developing a process to update material laws. OBM will be sending a letter to each state agency to request that they notify OBM of any material law changes. OBM also has a legislative update process that assists with the material law update process.

External Audit Update

Debbie Liddil, Chief Auditor, State Region, Auditor of State (AOS) and her staff provided the committee with the financial audit update.

Maria Jackson, Assistant Chief Auditor, provided an update on the FY 13 SOC 1 report for the State's Ohio Administrative Knowledge System (OAKS). The report was released on September 24, 2013 and contained an unqualified opinion. The related transmittal letter, which was submitted to DAS on November 5, 2013, contained a comment about user access roles, which she does not expect to include in the State Single Audit report. Ms. Jackson stated that they have met with OBM and DAS on the upcoming FY 14 SOC 1 audit and will be provided updated control narratives for that engagement.

Ms. Liddil stated that the financial audit of the CAFR began on October 21, 2013. This year her office also performed the audit of the Office of Loan Administration, which was a first time the audit has been performed by the AOS in several years. Although her staff experienced various delays, they have completed all agency support testing of the revenues and expenditures. They have sent reminder notices to the Independent Public Accountants (IPAs) of the state's components about the new requirement from the clarity standards regarding the need for the IPAs to update OBM and the AOS on the component's subsequent events through the State's financial statement opinion date. The AOS staff has been working hard to finish testing and additional staff has been assigned to the GAAP audit in order to complete the work.

A few changes from the financial statements required some additional review, such as the reporting entity changes involving the Ohio Water Development Authority, University of Cincinnati, and JobsOhio. There were some other issues to be considered such as the extinguishment of debt, unemployment compensation, and the franchising of liquor. The draft representation letter has been provided to Jim Kennedy for his review and distribution. The estimated opinion date has been moved to December 20, so the audit will be done by Christmas. The team has not found many audit issues at this point.

AOS Staff are shifting their focus to Single Audit testing related to the federal schedule and major federal programs. The opinion on the federal schedule will now be included with the opinion on federal major programs due to the re-issuance AOS needed to do with the EPA loan program. This change will eliminate the need to reissue the CAFR in the future if there are

issues with the Single Audit. Additional representations from OBM will be required for the February 20, 2014 issuance of the Single Audit report. The Medicaid testing process has improved.

Chairman DeMaria asked about the Office of Loan Administration. Ms. Liddil stated that they were a part of the Development Services Agency. Chairman DeMaria thanked Ms. Liddil for the AOS' great work and Ms. Liddil stated that she appreciated the Committee's attention to issues and Ms. Conkey's Audit Oversight Work Group. Mr. Bell mentioned that he and the Chairman provided the requested information to the AOS related to their fraud risk questionnaires.

Legal Update

Chairman DeMaria introduced Joy DeMarco, OBM's Associate Legal Counsel. Ms. DeMarco stated that Commission action is required regarding records retention. She provided four schedules for Committee consideration. Mr. Monahan asked why agendas were not included in the schedules. Chairman DeMaria stated that agendas could be considered part of the minutes. Ms. Vitaz asked if state agency information included in meeting presentations are considered in the proposed schedules. It was indicated that the committee would not be responsible for maintaining other state agency information; that would be the agency's responsibility. Ms. Vitaz moved to adopt the records retention schedules as drafted, Mr. Monahan seconded, all voted in favor and Chairman DeMaria declared the motion moved.

Ms. DeMarco also spoke to the Committee's question from the September 2013 meeting regarding the Committee's responsibility to the audit committees at Bureau of Workers' Compensation (BWC) and Lottery Commission. She stated that OIA and the State Audit Committee have the legal obligation to direct internal audits at the two agencies but it is acceptable to leverage the internal audit work performed at their respective internal audit departments.

Mr. Bell discussed the overview chart he prepared to provide context into the question about the flow of responsibility and communication. He mentioned that the relationship between OIA/State Audit Committee and BWC is long-standing, whereas the relationship with Lottery is new. Mr. Bell stated that OIA is involved with both BWC and Lottery's internal audit planning, as well as attending meetings and conducting an annual assurance review of the internal audit functions.

Chairman DeMaria expressed his appreciation for the overview summary. Mr. Hecht stated that the assurance letter is helpful but asked whether it protects the Committee. Mr. Bell stated that he feels that he is adequately engaged at BWC considering that he reviews BWC's charters, attends BWC meetings, and personally speaks with BWC's Audit Committee Chair on a regular basis. Mr. Bell stated the current relationship with Lottery is less formalized. Internal Audit directors from both agencies have recently left their positions. Mr. Bell has been active in assisting with their replacements. Mr. Hecht asked whether OIA should review BWC and Lottery's preliminary reports as opposed to the final reports. Mr. Bell mentioned that BWC and Lottery do not have the same level of legal protection in the Revised Code as OIA as to what is preliminary vs. final. Mr. Bell stated that he would have to consider the possible risk to auditor independence. The Committee requested that both BWC and Lottery internal audit present to

the State Audit Committee once a year. It was determined that September would be appropriate for both agencies to present their plan and results of their prior year plan. Mr. Bell stated that he would provide a summary at June meeting of OIA's plan to leverage both agencies' internal audit work.

CAE Update

Joe Bell, Chief Audit Executive for OIA, updated the Committee on the progress on the OIA annual plan for the second quarter of fiscal year 2014. He pointed out the new projects listed on the report. Regarding the statistics, Mr. Bell stated that his group was down to 20 staff during the second quarter, but still accomplished a good percentage of the plan. He stated that the goal is to accomplish 80% of the plan; 100% would be a reaching goal. Mr. Bell mentioned that 94% of the audit plan was accomplished in the prior year. He also stated that enhancing position descriptions to get best qualified personnel will take time.

Mr. Bell asked the committee if they wanted to see how OIA was performing in comparison to OIA's budget. He indicated more concern on how to address temporary staff shortages and what options and resources would be available in addressing these shortages. He stated that he would prepare a plan to address this concern. Mr. Monahan stated that it is unlikely that OIA has all needed resources and recommended that Mr. Bell establish relationships with a few companies that could provide these services. Mr. Hecht compared the staffing situation to that of a disaster recovery plan with certain strategies and different approaches. Mr. Monahan stated that he feels it is more important to get the audit plan completed rather than OIA be under budget on expenses. Mr. Bell stated that he will enlist the human resources assistance of Ms. Conkey to accomplish the plan.

Mr. Bell stated in regards to remediation, there were no outstanding high risk items to report.

Cindy Klatt, Chief of Quality Assurance, OIA, presented a memo to the Committee regarding her assurance review of BWC Internal Audit. She stated her conclusion that OIA is able to rely on the work performed by BWC Internal Audit. She noted her recommendation that BWC Internal Audit document their work in an electronic work paper format to aid with efficiencies and security of the work papers. She also noted that BWC Internal Audit has not had an external peer review, which is contrary to the standards established by the Institute of Internal Auditors (IIA).

Mr. Monahan expressed concern about the lack of an external peer review and asked if BWC Internal Audit had policies and procedures. Ms. Klatt indicated that BWC recently created policies and procedures based on the prior year's assurance review. Mr. Monahan suggested that all internal audit organizations in the State have the same policies and procedures. With that, quality assurance reviews would utilize the same basis. Mr. Bell agreed with the concept and wanted to consider the effect of this change. Mr. Monahan further stated that the quality assurance reviews performed at OIA could include projects from BWC and Lottery, so the external review could also include those two agencies, which would preclude the need of a separate external review and reduce overall costs.

Mr. Bell confirmed the independence of OIA staff. Ms. Vitaz asked if OIA staff were required to sign an independence confirmation, and Mr. Bell stated that OIA staff do sign an independence confirmation once a year. He also said that if independence changes occur, OIA staff are required to update the confirmation.

Mr. Bell stated that OIA's Internal Audit Charter is reviewed annually and that he included suggested language changes for the new entities under OIA's purview. He also suggested removal of language about what the Chief Audit Executive and staff cannot do, which is already prohibited by the IIA standards. Chairman DeMaria requested a motion to adopt the changes as set forth in the Internal Audit charter. Mr. Monahan moved to approve the revised charter, Mr. Hecht seconded, and all approved with no objections or questions to accept the Charter as presented.

The Committee paused their meeting for lunch at 11:49 a.m. and reconvened at 12:13 p.m.

Executive Session -- At 12:14 p.m., Chairman DeMaria stated a motion to move the meeting into executive session for the purpose of discussing confidential matters exempted from public disclosure under Ohio Revised Code Sections 126.48 and 149.433. Mr. Monahan seconded the motion and a roll call vote was taken and, there being 4 yeas and 0 nays, the motion was approved.

The Committee moved out of Executive Session at 1:34 p.m.

The Committee determined the following eight reports to be final public reports in accordance with Revised Code Section 126.48:

1. Development Administrative Services – Procurement Process
2. Department of Aging – Passport Incentive Payments
3. Environmental Protection Agency – District Office Check Handling
4. Environmental Protection Agency – Payroll Disbursement Testing
5. Department of Health – Grants Processing
6. Department of Mental Health Addiction Services – Office of Support Services
7. Department of Public Safety – Emergency Management Agency Operations
8. Department of Transportation – Non-Federal Revenue Process

Chairman DeMaria requested a motion to approve the eight public reports; Mr. Monahan so moved and Ms. Vitaz seconded. All agreed and the reports were approved.

Open Discussion

Finalize CY 2014 Audit Committee Calendar

The Committee agreed on the finalized dates for 2014 meetings – March 13, June 25, September 25, and December 11.

Mr. Monahan asked about meeting assessment and it was stated that Committee members will provide feedback about the meeting to Mr. Bell, who will in turn distribute those thoughts to the Committee members to help improve future meetings.

The meeting was adjourned at 1:40 p.m.

Open Items for March, 2014 meeting

1. Advise availability for future meetings.

Responsible Party: Members

2. Provide feedback on Committee meeting assessment

Responsible Party: Joe Bell/Members

3. Schedule periodic IT Optimization updates with State Chief Information Officer Stu Davis (June)

Responsible Party: Joe Bell

4. Develop macro statistics for previously issued audit observations (March)

Responsible Party: Joe Bell

5. Schedule BWC and Lottery Internal Audit to present to Committee (September)

Responsible Party: Joe Bell

6. Schedule David Brown from DAS to speak to Committee about state security issues (March)

Responsible Party: Joe Bell

7. Schedule BWC CIO to present to Committee about status of CORE (March)

Responsible Party: Joe Bell