The School Board of Broward County, Florida
AUDIT COMMITTEE

MINUTES OF AUDIT COMMITTEE MEETING

December 10, 2009

Mr. Steve Hurst, Vice Chair, called the Audit Committee meeting to order at 12:30 p.m. at the Kathleen C. Wright Building in the 1st Floor Board Room. Members and guests were introduced.

Members Present:

Mr. Anthony De Meo, CPA
Mr. Joey Epstein, CPA
Ms. Mary Fertig
Ms. Charlotte Greenbarg
Mr. John Herbst, CPA
Mr. Charles Howell, CPA
Mr. Roy Karlsen
Dr. Henry Mack
Mr. Ted Perrella, CPA
Mr. Neal Shapiro

Staff Present:

Mr. James Notter, Superintendent of Schools
Mr. Donnie Carter, Chief Operations Officer
Mr. Ben Leong, Chief Financial Officer
Mr. Henry Robinson, Treasurer
Mr. Patrick Reilly, Chief Auditor, Office of the Chief Auditor (OCA)
Mr. Dave Rhodes, Director Facility Audits, OCA
Ms. Delores McKinley, Director, Internal Accounts, OCA
Mr. Joe Wright, Facility Auditor, OCA
Ms. Vicki Hill, Facility Auditor, OCA
Mr. Mark Magli, Property Audit Supervisor, OCA
Ms. Patricia McLaughlin, Confidential Clerk Specialist C, OCA
Ms. Megan Gonzalez, Confidential Clerk Specialist B, OCA
Ms. Rhonda Schaefer, Inventory Audit Specialist, OCA
Mr. Bryan Erhard, Inventory Audit Specialist, OCA
Ms. Sharon Airaghi, North Area Superintendent
Dr. Leontine Butler, Central Area Superintendent
Dr. Joel Herbst, South Area Superintendent
Mr. Jeff Moquin, Support Operations
Mr. Oleg Gorokhovsky, Director of Accounting and Financial Reporting
Mr. Chuck Stanley, Executive Director, ETS
Ms. Melissa Grimm, ERP Project Director

Guests Present: Mr. Dan O'Keefe, Engagement Partner, Moore Stephens Lovelace, P.A.
Mr. Derrick Lomas, Moore Stephens Lovelace, P.A.
Mr. Manuel Garcia, CPA, GLSC & Company, PLLC
Ms. Barbara Zembron, PTA
Ms. Patricia Mazzei, Miami Herald
Ms. Akilah Johnson, Sun Sentinel

Old Business

A motion was made to approve the minutes for the October 22, 2009 Audit Committee meeting with one revision on page 6. Motion carried.

Moore Stephens Lovelace, PA – Comprehensive Annual Financial Report (CAFR) – June 30, 2009

Mr. Dan O'Keefe presented the CAFR and mentioned that this report was actually prepared by District staff. "Our responsibility is to audit that document. The only item we have remaining before we can issue our report is to receive a representation letter that I understand I should be receiving pretty quickly. The Auditor General is waiting for us to issue our report, as they will be relying on our work this year for their audit purposes. They have already begun working on the Single Audit Report. I'd like to bring your attention to the Financial Section; specifically, a document called The Report of Certified Public Accountants. This is really the item that we issue for you. This report is an unqualified opinion; it tells you the scope of the engagement, that we performed the audit in accordance with generally accepted auditing standards and government auditing standards which apply to School Districts. You will see the certificate of achievement on page xiii." He provided a presentation of the financial reports, including Management's Discussion and Analysis, and Notes to the Financial Statements that are important parts of the CAFR. He complimented District staff by stating that this CAFR was one of the best in the State. He discussed the Statement of Net Assets, stating that this is basically a full accrual balance sheet that identifies a $90,000,000 deficit fund balance, which is not a desirable position to be in. He pointed out on the Statement of Activities page that the change in net assets was a decrease of $142,732,000, mainly due to less revenues coming into the District, which occurred in other Districts, as well. He explained the fund balance under the modified accrual method of accounting, which in this method, the undesignated general fund balance is $77,607,000. He emphasized the difference in reporting using the Statement of Net Assets and Modified Accrual method of reporting financial information. He also provided a general overview of the reconciliation of the government fund balance sheet to the net assets. He pointed out on Page 28 that the general fund expenditures were greater than the revenues, resulting in a $30,942,000 decrease in the fund balance.

Dr. Henry Mack stated he was concerned that expenditures exceeded revenues, resulting in a significant decrease in the fund balance. He asked what the administration was doing to correct this situation. He questioned the overtime expenditures discussed in previous Audit Committee meetings and asked what was being done about that situation.

Mr. Ben Leong replied concerning the $30,000,000 expenditures that exceeded revenues brought into the District was due to economic conditions of the State. He also stated that the 2009-10 current year would be more severe than the 2008-09 fiscal year. He added “For this year, the District received $127,000,000 less in tax revenues, compared to last year.” He stated that the District would be looking at expenditures of every location and would look at them from a profit and loss (P&L) position, especially in the major cost centers, such as Transportation, Maintenance, etc. to monitor and reduce future expenses. Mr. Leong discussed different phases, such as analyzing reserve balances, expenditures and ways of aligning services with student achievement.

Dr. Mack asked about overtime expenses and the $2 million that PPO allegedly provided in work orders to the Food Service Department. Discussion followed.

Mr. James Notter asked Mr. Leong if the $30 million was impacted by some of the mid-year cut. “If so, don’t you start to go into your fund balance?”

Mr. Leong replied “Yes, the State of Florida adopted the budget. By State law, the State must have a balanced budget. Therefore, there was a proration for the District called a mid-year budget hold back, which amounted to about $36 million and contributed to the $30 million deficit. Also, salary increases added to the budget deficit, so we had to cut expenditures more than the State cuts, to allow for these increases. The mid-year budget cut will occur again this year. These factors have had a negative effect on the fund balance.” Discussion followed pertaining to the budget situation and Mr. Notter asked for the assistance and guidance of the Audit Committee during these critical times.

Ms. Mary Fertig added “There are several areas where the Auditors have identified monies that could be saved by different business practices or monies that could be collected because we overpaid. In the final analysis, we should look at saving or recouping money that has been inadvertently overpaid.”

Ms. Charlotte Greenbarg stated “I would like to discuss what the numbers are telling us. As a retired business person, I’m looking at the number of students, which has declined significantly. When you see the number of students declining, that would tell me that I had to do something from 2005 on, so it shouldn’t be a surprise when there is a $30 million problem.”

Discussions followed regarding the amount of debt the District currently has incurred.

Mr. Leong and Mr. Henry Robinson provided information about the current percentage of debt and allowable capacity of debt that can be held.

Mr. Ted Perrella referred to page 11 and asked if it was correct that the District did not have a balanced budget.

Mr. Leong stated that “By law, we are required to have a balanced budget. This schedule does not include transfers and revenues that have not yet come in; therefore, it is not correct to say that we didn’t have a balanced budget.”

Moore Stephens Lovelace, PA – Management Letter for the Year Ended June 30, 2009

Mr. O’Keefe began “The first report, required by Government Auditing Standards, is in relation to the Financial Statement Audit itself. One requirement is to assess control risks and test controls and also, you must consider the compliance risks as related to the financial statements. This report is unqualified; we didn't find any significant deficiencies or material weaknesses. The Management Letter on page 3 contains items that are not material weaknesses, significant deficiencies or material violations of laws and regulations, but are still important. We have provided you with the current year comments, which are coded according to year end (09) and there are four new comments and a summary of the prior year comments. The prior year comments outstanding have all been implemented, with the exception of two. The explanation of the status of those two items is in this report."

Dr. Mack asked about the value of the physical inventory account for gasoline.

Mr. O'Keefe answered "$5 million".

Dr. Mack asked "If we filled up every District owned vehicle, how much would that amount to? Would that be $5 million?"

Mr. Oleg Gorokhovsky answered "Probably a half million dollars".

Mr. Leong explained that the Auditing Department conducts an inventory at year end. "They look at the physical inventory, calculate it, and when comparing the Compass system to the General Ledger, there was a difference of $5 million. For some reason, the accounting record was not properly recorded."

Dr. Mack replied "Apparently the accountability for fuel has been unsatisfactory. You stated in the Management response that you will reconcile Compass and SAP and you are going to complete your Business Practice Bulletin by 2010. I'm speaking to the Administration now. I'd like for Melissa Grimm to explain how SAP relates to this item."

Ms. Melissa Grimm stated "Compass is the work order system; it was not part of the BRITE project that was supposed to be in Phase 2, which for various reasons, was not completed. As a result, when they were issuing or receiving fuel, initially they had to make double entries (entering into SAP and also into Compass). Due to the delay with Wave 2, it was decided to build an interface that would allow them just to enter their information into Compass, but that interface was only developed in December, 2008. The interface was only in existence for six months of the last fiscal year. The double entry process was performed for six months and then the interface was implemented. Today, the interface is working correctly; initially there were some problems. There are no issues at this time."

Mr. Patrick Reilly stated his staff performed a physical inventory of all tanks to determine the number of available gallons of fuel on June 30, 2009 and found the dollar value of the fuel on-hand as of June 30, 2009, using invoices from the last purchase made at the end of the year. He added "The adjustment was made to the SAP Inventory account to reflect physical count values."

Mr. Joey Epstein asked if some of this could be cumulative from the prior year, causing the out of balance condition to roll over into this year.

Mr. Reilly stated "No, a physical inventory and adjustments were made in June, 2008, and I would have noted a large adjustment."

Mr. John Herbst stated that in this case, there appeared to be an internal control mechanism that was not functioning as intended. He stated he was curious as to why the external auditor did not consider a five million dollar variance a significant deficiency.

Mr. O'Keefe stated "We looked at it from a couple of different ways. First, we were talking about $5 million on a $3 billion balance sheet. The $5 million sounds like a lot when you talk about the District, but when you run it through our materiality criteria as we apply it to the financial statements, it actually fell below the materiality threshold. We still felt it was significant enough to report it in the Management Letter. That is our opinion and Auditor judgment."

Mr. John Herbst stated he understood in the context of the financial statements, when taken as a whole, that it would not be material for an adverse opinion. He added "But, in terms of your internal control evaluation, certainly it is a control deficiency and under SAS 112, this would rise to the level of a significant deficiency."

Mr. O'Keefe stated "Again, it is Auditor judgment. We debated it heavily and still concluded it should be reported."

Dr. Mack stated "We don't care what the threshold is; the Audit Committee is concerned about any amount over $.99."

Mr. Perrella asked about the requirements of SAS 70 and whether the District received a SAS 70 report.

Mr. Jeff Moquin stated "There are two third party administrators for general liability and workers' compensation. The workers' compensation did not have a SAS 70 report. The reason the workers' compensation administrators did not have the SAS 70 report is due to the change in their informational system, in order to provide the data that we require. We implemented a brand new workers' compensation program. We are the flagship program and the vendor is changing their processes to meet our needs and provide for us. The vendor is contractually responsible to provide the report and they will be providing a SAS 70 report."

Dr. Mack stated he wanted to encourage staff to complete the audit exception noted in the report. He asked if Mr. Notter could provide an update to let the Committee know what the plan was to take care of both sets of observations of the external auditors.

A motion was made to approve the CAFR and Management Letter and transmit the reports. The motion was seconded and approved.

Follow-Up Items

Property and Inventory

Mr. Reilly presented an update on the Property and Inventory issues. He stated that a School Board workshop was held on November 24, 2009. Many issues concerning inventory audits and audit procedures were discussed. He continued "Specifically, it was agreed that a Business Practice Bulletin will be created that will encompass all procedures relating to the purchasing, monitoring and surplusing of equipment at all District locations. Mr. Mark Magli provided a

PowerPoint and emphasized during the workshop the importance of downloading the PNI811 by District staff and discussed the benefits of the inventory database to obtain various forms for managing property, (i.e. property passes, surplus transfer forms, etc.)"

Ms. Greenbarg congratulated Mr. Magli and the OCA staff for their tremendous work.

Mr. Mark Magli thanked his staff and introduced them.

Ms. Greenbarg asked about the timeframe for the completion of the Business Practice Bulletin.

Mr. Reilly replied that it was scheduled to be ready in March, 2010.

Ms. Greenbarg asked if there were any penalties for non-compliance.

Mr. Reilly answered "That would be an HR issue."

Mr. Donnie Carter spoke about Best Practices that have been implemented in the schools that would be implemented in the Departments. He also addressed Ms. Greenbarg's comment regarding the two page document from the Administrators' representative, in which she had some concerns with the inventory processes. Mr. Carter said he would review the issues.

Ms. Fertig asked if the penalties for non-compliance would be consistent for schools and departments.

Mr. Steve Hurst asked how long unlocated items remain on the unlocated list.

Mr. Reilly replied "Two years".

Discussion followed.

Mr. John Herbst asked if it was common that some of the unlocated items that were surplused were the result of the paperwork not being completed or maintained.

Mr. Magli said "Yes".

Ms. Greenbarg stated that many schools are doing the process correctly.

Follow-Up Item #2

Overtime Expenditures

Mr. Reilly stated that a School Board workshop was held regarding the changes that the District planned to make relating to overtime payments. "Currently, there is a group working to revise School Board Policy 4300.1, which will clearly define everything related to overtime (primary and secondary) and procedures for determining overtime hourly rates."

Dr. Mack asked "Are you dealing with the issue, for example, if I am a pay grade 31 and I'm driving a bus later in the day, am I paid at the level of the bus driver or my primary pay rate?"

Mr. Reilly replied "Some people are receiving overtime at their primary rate for their secondary job, but management is planning to change this practice. There are several options under the Fair

Labor Standards Act (FLSA) that can be implemented (for example, a blended rate). Per discussion with Melissa Grimm, it has not been determined which method will be used."

Agenda Items

Internal Audit Reports – Audits of the Internal Funds of Selected Schools in the North, Central and South Areas

Mr. Reilly stated "There were twenty-one schools audited; nineteen of them complied with all prescribed policies and procedures. There were two schools that had exceptions related to the now discontinued Principal's Discretionary Fund, delinquent loans and some activities related to missing funds, and procedures for ticket sales that were not properly performed."

Ms. Fertig requested an explanation from the Area Superintendent regarding the use of monies placed into the Student Government account for faculty parties.

Ms. Sharon Airaghi stated that would not be occurring in the future.

Ms. Fertig requested that the issue be addressed at the Principals' meetings throughout the District.

Dr. Mack stated "This activity looks like money laundering. There are policies in place to clarify the procedures for handling deposits and disbursements in the Internal Fund accounts." He asked that the Area Superintendents make it a priority to ensure that this practice be discontinued.

Ms. Greenbarg stated "On page 59, on the response 'It was the opinion of administration and voted on by student government' probably tells the whole story. If the students understand that's what the administration wants, that's the way the students will vote. I think that response is an unintended consequence that shouldn't have been there. I'm not pleased to see that response from a Principal".

Ms. Airaghi stated that had been addressed.

Mr. Hurst asked about the band uniform loans and requested a listing of each school's outstanding debt to the General Fund.

Mr. Reilly stated he would follow up on that item.

Discussion followed related to band uniform loans and payment options.

Ms. Greenbarg asked relating to page 69, #5, "Why did the Principal say that it was not recommended in the past to perform an SIU investigation of the former Athletic Director, who seems to be involved in the whole thing? One retired, one was terminated. The Athletic Director just transferred somewhere else. Do we know why the Area would recommend that?"

Dr. Leontine Butler stated that she had met with Delores McKinley and that this employee had been terminated.

Ms. Greenbarg thanked Dr. Butler.

Mr. Hurst asked for a motion to transmit. Motion carried.

Internal Audit Report – Property and Inventory Audits of Selected Locations

The Committee discussed the audit report, which contained thirty-five locations; twenty-one locations complied with prescribed policies and procedures. There were fourteen locations that contained audit exceptions consisting of unaccounted for property and the failure to follow some prescribed rules.

Ms. Fertig questioned the procedures in place for departments that don't fall under the direction of an Area Superintendent, specifically, the three Area offices. She stated "I want to know who follows up with those departments".

Mr. Reilly stated "It is basically the person to whom they report. The Principals report to the Area Superintendents; for example, PPO would report to Mr. Carter, etc."

Ms. Fertig continued "Let's look at the three departments that have repeat exceptions, Food Service, Pre K, and Transportation; who's following up on these?" She stated that the schools have shown improvement and wanted to ensure that the Departments are being monitored effectively.

Discussions followed and it was determined that Transportation would be under Mr. Carter; Pre-K would be handled by Dr. Smiley.

The Property and Inventory Audit report was discussed during the follow up discussion items.

Mr. Hurst asked for a motion to transmit. Motion carried.

Recap of Charter Schools and Status Update

Mr. Reilly stated "We will be discussing all the Charter Schools at this meeting, with the exception of those Charter schools that are run by Governmental entities. We made a matrix of the schools this year that have financial emergencies. With the changes in the State requirements and Florida statutes, if a Charter school is considered to be in a financial emergency (in most cases, having a negative fund balance or negative total net assets), the school must have a recovery plan in place. We met with these 12 Charter schools on November 19 and 20, 2009 and discussed their plans to work on reversing their deficit fund balances and financial emergencies, as identified by the State. There were some schools that were on the list last year, but not this year, since they are no longer in a financial emergency status, but there are a couple of schools who have remained in a financial emergency situation for several years. Those are the ones we'll be meeting with again in January with our Charter School Department. In the back of this report, we listed all the reports that we received. There were four schools that did not meet the September 30, 2009 deadline to submit their financial audits completed by outside CPA firms. This was a concern and is a violation of their agreement with the District. We met with them and gave them a timeline to have those reports available to us prior to the next meeting. I believe that two of them were received yesterday by the Charter School Office, leaving only two remaining. On page 13, you can see which schools are in a good financial position and those in a financial emergency situation and those who haven't turned in their reports to date."

Mr. Hurst asked Mr. Reilly if there would be a follow-up. Mr. Reilly stated that we would be meeting with the Charter schools at the end of January, 2010.

Mr. Anthony De Meo asked Mr. Reilly to explain what the Audit Department's involvement is with the Charter schools.

Mr. Reilly replied "We assist the Charter School Department mainly with the financial and audit functions. We recently assisted them with the close out of a Charter school. We work with fixed assets to ensure that when a Charter school closes, the assets purchased with FTE money revert back to the District. We review their quarterly financial statements and review in depth their annual financial reports. We correspond regularly with the Charter schools when they have questions regarding their emergency plans and give recommendations and suggestions on internal control procedures, etc."

Discussion followed.

Mr. John Herbst asked why he didn't see "going concern" statements by the Auditors for the various Charter schools that show deficit balances year after year.

Mr. Reilly answered "There were a couple of years where they were showing that in the reports; what happens in many cases is that the sponsor or the Board promises (in the form of a written document provided to the external auditor) that they will "step up" financially, when necessary. This suffices to the auditors that the "going concern" is not totally a true "going concern", since they have a sponsor to cover them if need be."

Mr. John Herbst stated that he had seen these types of arrangements, where often times the funding does not materialize when the money is needed.

<u>Other Comments</u>

Mr. Hurst asked Ms. Greenbarg if she would be having an orientation meeting for the new Audit Committee members and asked that the Audit Department send a copy of Dr. Mack's annual report to the new members.

Ms. Greenbarg stated that she would set up the meeting.

Ms. Greenbarg asked about obtaining a listing of the cadre attorneys and their expertise along with the amounts paid to each attorney and how much money each attorney was able to recover for the District.

Ms. Fertig asked about auditing capital expenditures; specifically, monies that have been allocated or encumbered on projects that have been completed, in which the unused monies remain encumbered in the project's budget. She felt that an audit of this area could possibly identify money that could be available from projects that have been closed out.

Mr. Notter stated that the District also had some projects that have been designed that had been placed on hold.

Mr. Reilly stated "We had identified purchase orders that should be closed out that had remaining funds on them that could have been put back into the Capital Budget."

Mr. Notter stated that the audit should be done before June 2010. He thanked the Audit Committee for their service to the District.

Ms. Greenbarg stated that the Facilities Task Force had pursued this issue and Mr. Omar Shim looked into the matter and found $38 million that the District could utilize that they were unaware of in the Capital Project funds.

Meeting adjourned at 2:25 p.m.