



**STATE AUDIT COMMITTEE**

**WEDNESDAY, DECEMBER 18, 2019, 10:00 A.M.  
RHODES STATE OFFICE TOWER  
30 EAST BROAD STREET, 35<sup>TH</sup> FLOOR, JUPITER/SATURN CONFERENCE ROOMS  
COLUMBUS, OHIO 43215**

Members Present: Larry Long  
Andrea Weaver  
Ann Gabriel  
Glenn Roberts  
David Beule

**Call to Order**

Chairman Larry Long called the meeting to order at 10:04 a.m. Chairman Long acknowledged the committee members in attendance and asked the newest member, Glenn Roberts, to introduce himself. Mr. Roberts provided an overview of his background, including his military and accounting experience. Michael Babin, OBM Associate Legal Counsel, then issued the Oath of Office to Mr. Roberts.

**Approval of Minutes**

Mr. Beule moved for the minutes of the meeting held September 19, 2019 to be accepted with no additions or corrections. Ms. Weaver seconded the motion. All committee members voted in favor of approving the meeting minutes with no objections.

**OBM Financial Reporting Update**

Linda Shook, OBM Financial Reporting Manager, discussed the joint timeline for the completion and audit of the FY 2019 Comprehensive Annual Financial Report (CAFR), as well as recent deliverables related to the FY 2019 State Single Audit. She mentioned after the CAFR opinion date, the OBM financial reporting team would be working on finalization for the State Single Audit, with the goal of meeting the expected audit opinion date, February 19, 2020.

Jim Kennedy, OBM Senior Deputy Director for Services and Operations, presented summary highlights from the State's FY 2019 unaudited financial statements and compared them to results over the last five years. The three areas Mr. Kennedy highlighted are: changes in general fund balance, budget stabilization fund balance, and State's net position for the total primary government. Mr. Kennedy noted the State's General Revenue Fund (GRF) balance increased to \$7.7 billion after having maintained an average balance of approximately \$5 billion for the past five fiscal years; the reason for the increase being higher than expected tax revenue and a decrease in Medicaid expenses. Mr. Kennedy noted this is the highest GRF balance ever for the State. He also noted the State's Budget Stabilization Fund (BSF), commonly referred to as the "Rainy Day" fund, is a part of the GRF. The balance of the BSF is an indicator of how the State

would cope in a recession period. Ms. Gabriel asked about whether the State had a funding policy for the BSF. Mr. Kennedy responded the State's BSF has a set ceiling of 8.5% of the prior year tax revenues, which for FY 2019 would equate to approximately a \$2.9 billion ceiling; the current FY 2019 BSF balance is \$2.69 billion. Chairman Long inquired if the accounting of Medicaid funds is handled through the GRF. Mr. Kennedy confirmed that all the Medicaid program expenses and revenue are paid out of and deposited into the GRF, so if there is a reduction in Medicaid expenses, as there was in FY 2019, it helps the GRF balance.

The State's unrestricted negative balance decreased approximately \$1.5 billion to \$11 billion, after a spike in FY 2018 (\$12.7 billion). The spike in FY 2018 was due in large part to new Other Post-Employment Benefits (OPEB) reporting requirements that went into effect. While Mr. Kennedy said the \$11 billion may appear alarming, approximately \$9 billion of it is due to the OPEB liability (\$2.9 billion) and Net Pension liability (\$6.1 billion). Mr. Kennedy also pointed out that the State has historically had a negative unrestricted balance due to the general obligation debt it issues on behalf of local governments and colleges, in which the related asset is on the local entity's statements and not the State's government-wide statements. Mr. Kennedy also mentioned that he compared Ohio's unrestricted balance to six other states with comparable tax revenue and population. Chairman Long asked if there was any data as to how Ohio compared in its funding of the local government and college debt; Mr. Kennedy responded he did not know, and stated that other states may not fund their local governments the same way as Ohio. Ms. Gabriel asked if pension liability was comparable across the other states; Mr. Kennedy responded that because Ohio's Public Employee Retirement System (OPERS) is a multiple-employer retirement system, of which the State is just one of many employers, it is not comparable. Mr. Kennedy also clarified that the Net Pension Liability amount reflected on the State's financial statements is just the State's portion and not all the retirement system's liability.

### **External Audit Update**

Steve Gibson, Senior Audit Manager of Information Systems Audit from the Auditor of State (AOS) State Region, discussed the results of the FY 2019 SOC-1 audit for the Ohio Administrative Knowledge System (OAKS), covering the period July 1, 2018 through March 31, 2019. A modified opinion, dated September 25<sup>th</sup>, was released on October 21<sup>st</sup>. The modified opinion was a result of two control objectives not operating effectively. In conjunction with the SOC-1 report release, a transmittal letter was issued to management detailing several recommendations based on the work performed. All items are being considered by the financial auditors for possible inclusion in the State of Ohio financial audit of the CAFR.

Debbie Liddil, Chief Auditor from the AOS State Region, provided a status of the State of Ohio CAFR audit and Single Audit. Completion of the CAFR audit is in the final stretch, and barring any issues, the opinion is planned to be issued December 20, 2019. The agency testing of revenues and expenses required to be done to support the CAFR audit is substantially complete, with the audit team wrapping up one final substantial piece of testing before finalizing the reports. Along with the CAFR opinion, a Yellow Book letter will be issued to include any report comments at the

financial statement level related to testing issues identified. Ms. Liddil also noted that because they rely on several IPAs to perform work related to the State of Ohio audit, they have received those IPA audit reports and are in the process of receiving the subsequent events letters which are due December 18<sup>th</sup>. The representation letter, which was presented to OBM for distribution to the Governor for his signature on December 6<sup>th</sup>, is expected back to the Auditor of State by December 20<sup>th</sup>. Looking ahead to next year, the implementation of GASB 84 will have a significant impact on the financial statements.

Ms. Liddil noted that because of the timing of the December audit committee meeting date and the Auditor's release of the CAFR audit report, she is unable to provide the Committee with the results of the audit until the next scheduled audit committee meeting. Going forward, she asked the Committee to consider the possibility of adjusting the December audit committee meeting so that the results of the financial statement audit can be shared with the committee members timelier. Mr. Long thanked both Ms. Liddil and Ms. Klatt, noting that the committee members could talk with Ms. Klatt later as to the possibility of moving the December meeting date.

With the financial statement audit wrapping up, Ms. Liddil stated the field staff are now focusing on single audit testing of 26 major programs at 11 separate state agencies. AOS intends to issue an opinion and release the Single Audit on February 19<sup>th</sup>. The results of the State of Ohio CAFR and Single Audits will be discussed at the March State Audit Committee meeting.

Chairman Long asked Ms. Liddil about the differences between agreed-upon procedure (AUP) reviews and financial statement audits. Ms. Liddil responded that AUPs are performed under different standards and are typically narrow in focus for what they are trying to achieve. For AUPs, the auditor and client develop and agree to the procedures to be performed to satisfy the user's (client) specified purpose for the procedures. Any report issued as a result of an AUP engagement must include a disclaimer that the procedures and report are only intended for the specified users named and for the purposes defined within the report. Ms. Liddil gave the Treasurer of State's Sinking Fund as an example of an AUP engagement that rolls into the State of Ohio financial statements. The AOS, as the intended user and requester of the engagement, defines the procedures the IPA performs over the Sinking Fund. Ms. Liddil indicated there are limitations and restrictions to the timing of when an AUP engagement can be performed at a state or local government entity in place of a financial statement audit. Ms. Liddil also clarified that auditors are not expressing any assurance on AUP engagements; it is up to the user(s) of the report to draw their own conclusions based on the results of the procedures.

### **CAE Update**

Ms. Klatt provided an update to the committee members on the FY 2020 second quarter's activities by discussing the Annual Audit Plan status including any plan changes, staffing levels, percentage of engagements completed per the Annual Plan, and remediation dashboards covering all outstanding observations from prior issued assurance engagements. Because of the large volume of outstanding observations, Ms. Klatt noted that the internal audit teams have evaluated the long-standing items to determine if action was being taken or if the agencies were

essentially accepting the risk through inaction. In most cases, Ms. Klatt indicated it was found agencies are acting on the items and not accepting the risk, but remediating the observations is taking longer than the agencies initially planned.

As required by IIA standards, Ms. Klatt confirmed to the committee members the independence and objectivity of the internal audit activity, as well as the independence of the internal audit employees. Ms. Klatt responded to Ms. Gabriel's inquiry about training provided to audit staff related to this matter, indicating the OBM Legal Office provided training in the past and that she would follow up to inquire about further training. Mr. Roberts inquired about whether committee members need to sign any confidentiality forms, to which Mr. Mike Babin, OBM Associate Legal Counsel, responded that the oath taken upon becoming a State of Ohio Audit Committee member is sufficient. Ms. Klatt also noted that as it relates to committee member independence, she inquires of any conflicts at the start of each member's term; if an independence issue is noted with an agency under Internal Audit's oversight, the audit committee member is walled off from any activities or communication related to that agency.

Ms. Klatt then presented the draft State Audit Committee charter to the committee members for approval. Ms. Klatt noted that while there were only a few minor edits to the document from last year, the Committee Charter is required to be reviewed and approved by the members annually. There were no additional edits or objections by the committee members. Ms. Weaver moved to approve the State Audit Committee Charter as revised and Ms. Gabriel seconded the motion. All members unanimously approved the revised State Audit Committee Charter.

Ms. Klatt informed the committee of the calendar year 2020 meeting dates: March 25, 2020; June 23, 2020; September 23, 2020; and December 17, 2020. The committee members were not aware of any conflicts with these dates.

*Executive Session* -- At 11:20 a.m., Chairman Long moved that the Committee enter into executive session to discuss confidential matters exempted from public disclosure under Ohio Revised Code Sections 126.48 and 149.433. Preliminary reports of the Office of Internal Audit of the Office of Budget and Management and reports that constitute a security or infrastructure record are required to be kept confidential under Ohio law. Ms. Gabriel seconded the motion to move into executive session and a roll call vote was taken; Ms. Gabriel, Ms. Weaver, Mr. Beule, Mr. Roberts and Chairman Long all approved. The Committee moved out of Executive Session and paused for lunch at 11:48 a.m. before reconvening with all five members present at 12:24 p.m.

*Executive Session* – At 12:25 p.m., Chairman Long moved that the Committee enter into executive session for the purpose of continued discussion on confidential matters exempted from public disclosure under Ohio Revised Code Sections 126.48 and 149.433. Preliminary reports of the Office of Internal Audit of the Office of Budget and Management and reports that constitute a security or infrastructure record are required to be kept confidential under Ohio law. Mr. Roberts seconded the motion. A roll call vote was taken: Ms. Gabriel, Ms. Weaver, Mr. Beule, Mr. Roberts and Chairman Long all approved. The Committee moved out of Executive Session at 1:40 p.m.

Chairman Long moved that the State Audit Committee accept the assurance reports submitted by the Office of Internal Audit; the motion was seconded by Mr. Beule and all attending members approved the motion. Pursuant to the motion, the following fourteen assurance reports were accepted in accordance with Revised Code Section 126.48:

1. Department of Administrative Services – Ohio Data Analytics: Security Review
2. Department of Agriculture – Western Lake Erie Basin Program
3. Department of Commerce – Unclaimed Funds Investments
4. Development Services Agency – Third Frontier Grant
5. Department of Developmental Disabilities – Agency Procurement
6. Department of Education – EdChoice Scholarship Expansion
7. Department of Education – Access Controls
8. Department of Health – Drug Overdose Grants
9. Department of Job and Family Services – Agency Procurement
10. Department of Natural Resources – Dam Fee Collection and Permitting
11. Department of Public Safety – Payroll Process
12. Department of Taxation – Personal Income Tax Fraud
13. Department of Transportation – IT Vendor Management
14. Bureau of Workers’ Compensation – IT Change Management

### Open Discussion

Ms. Klatt informed the committee members that representatives from the Department of Commerce were present to discuss the securities enforcement audit that was included in the FY 2020 audit plan. Ms. Klatt gave a brief background noting that in the FY 2019 audit plan, Internal Audit identified an audit over the securities enforcement function. In the planning meeting for that engagement, Commerce expressed concern over Internal Audit conducting the engagement. The audit was deferred to FY 2020 as OBM and Commerce legal counsel discussed Commerce’s concerns. Without coming to agreement on Internal Audit performing the engagement, Commerce was requested by OBM Director Kimberly Murnieks to personally present their concerns to the State Audit committee. Chairman Long welcomed the Commerce visitors.

Pete Thomas, Department of Commerce Chief Legal Counsel, and Andrea Seidt, Department of Commerce Securities Commissioner, introduced themselves and thanked the Committee for giving them the opportunity to speak on the matter of the securities enforcement audit. Mr. Thomas told the Committee their concern with the audit had to do with confidentiality of law enforcement and criminal investigation information. While Mr. Thomas and Ms. Seidt noted that Internal Audit does have some authority to keep certain documents and audit reports confidential

under Ohio Revised Code sections 126.48 and 149.433, they do not feel those adequately protect the securities enforcement activities that would be within the scope of the planned audit. Mr. Thomas and Ms. Seidt discussed the timeline leading up to their speaking on the matter in front of the Committee, starting in May 2018 when Internal Audit attempted to scope out the engagement, continued discussions regarding Commerce's concern with the scope due to the confidentiality of the information. In late fall 2018, Commerce's Securities Division reached out to other law enforcement bodies within the State, including Bureau of Criminal Investigations, Ohio State Highway Patrol to get their input as it pertained to allowing such an audit to occur with little provisions for maintaining the confidentiality of the information gathered during the audit. In November 2018, Commerce suggested requesting an attorney general opinion on the matter. Mr. Thomas noted that he joined the Commerce legal division as Chief Counsel in January 2019, at which time he met with Joy DeMarco, OBM Chief Legal Counsel, to discuss the issue and obtain OBM's perspective on the matter.

Mr. Thomas acknowledged OBM Internal Audit has proposed alternatives such as reviewing closed files, but Mr. Thomas explained his belief that the Securities Division's confidentiality statute under Revised Code Section 1707 is broader than the public record law under Revised Code Section 149.433. Additionally, Mr. Thomas stated there is a Supreme Court decision that indicates Revised Code Section 1707 supersedes Revised Code Section 149.433 because the latter was passed later in time. Mr. Thomas and Ms. Seidt suggested developing a working group with other law enforcement agencies of the State and Internal Audit to craft proposed legislative change that would allow this audit and other similar enforcement-type audits to move forward. Ms. Seidt also stated there are criminal penalties associated with sharing confidential information with Internal Audit that could be publicly released in a public audit, which presents a major liability to the Department of Commerce, as well as personal liability to the agency employee(s) who authorized the access to Internal Audit. Ms. Seidt indicated there is probably a way to get to an agreement with Internal Audit on being able to complete the securities enforcement audit, but it was her position that it should require working with the law enforcement groups to evaluate., Mr. Thomas thanked the Committee for giving them the opportunity to share their position on why the Department refused to allow the audit to proceed as it stands.

Chairman Long stated he had concerns with the department's denial as it gives the appearance of trying to hide something, which Mr. Thomas and Ms. Seidt acknowledged. Chairman Long also inquired as to the authority the Inspector General's Office has as it pertains to these types of law enforcement records. Ms. Seidt indicated the Inspector General's Office has one of the most protective confidentiality statutes in the State, so Commerce knows that confidential law enforcement records they provide to the Inspector General's Office are protected and cannot be released based on a records request. Ms. Gabriel asked if the solution is ensuring the results of the audit would remain confidential, which Ms. Seidt indicated while she thought that was the solution, she did not think it was that simple as all the other relevant parties involved who release confidential information to Commerce as part of their securities investigations would also need to agree to it.

Chairman Long asked Ms. Klatt for comments. Ms. Klatt stated that regarding Commerce's argument of public versus confidential record, Internal Audit had thought there was adequate reason to consider that it would be a confidential report and have the associated work papers protected as well, but the final determination of confidentiality is made by OBM legal. In deciding to keep the project on the FY 2020 audit plan, Internal Audit felt there was enough risk in the securities enforcement process to keep it as a planned audit and not substitute it for one of the public-facing aspects of the enforcement process proposed by Commerce that presented less risk. Outside of the initial discussions held with Commerce when trying to scope the engagement in the fall of 2018, Internal Audit has not been directly involved in this issue. Instead, both agency legal counsels have been working to resolve this matter.

Chairman Long proposed three approaches: 1) both parties walk away from the audit; 2) Commerce acknowledges and signs off on a statement indicating they understand and accept the risk of Internal Audit not being able to perform an audit over the area; and 3) developing a working group to come to acceptable resolution for moving forward. Chairman Long asked Ms. Klatt to relay the discussion and the approaches with OBM Director Kimberly Murnieks. Ms. Klatt responded that while these approaches offer three separate options, one action item that would need to be taken regardless of the other two options would be the documented acceptance of risk. Ms. Klatt clarified this would involve something from Commerce to memorialize the fact that Internal Audit is not performing the audit because Commerce does not want it to occur and that Commerce is accepting the risk of the securities enforcement processes not being audited. Mr. Thomas and Ms. Seidt responded they would share this information with the Director of Commerce.

Mr. Roberts encouraged Internal Audit to take whatever measures necessary to make certain that confidential information is not maintained within the working papers to minimize exposure in the event of an unauthorized access to the audit working papers. Ms. Klatt responded that Internal Audit has taken measures to limit any confidential information contained in audit work papers, and if such information is needed as part of the audit, the information is later redacted or marked confidential within the work papers. Chairman Long then thanked Mr. Thomas and Ms. Seidt for sharing their concerns with the audit committee.

Ms. Klatt provided the Committee with a summary of items planned for the March audit committee meeting, including the State CIO, Ervan Rodgers, to provide an update on the State's Office of Information Technology. As required by the Internal Audit Standards, Ms. Klatt will also provide the committee members with an update on how Internal Audit is complying with the Standards.

The meeting was adjourned at 2:13 p.m.

**Open Items for March 25, 2020 meeting**

None.