

**CITY OF COLUMBIA
AUDIT COMMITTEE MEETING MINUTES
JUNE 4, 2008 – 2:00 P.M.
CITY HALL - 1737 MAIN STREET**



The Audit Committee met on Wednesday, June 4, 2008 in the City Hall Council Conference Room located at 1737 Main Street, Columbia, South Carolina. The Honorable Mayor Robert D. Coble called the meeting to order at 2:27 p.m. The following members of the Audit Committee were present: The Honorable Anne M. Sinclair, The Honorable Daniel J. Rickenmann and The Honorable Kirkman Finlay III. The Honorable Sam Davis joined the meeting at 3:05 p.m. The Honorable E.W. Cromartie, II and The Honorable Tameika Isaac Devine were absent. Also present were Mr. Charles P. Austin, Sr., City Manager and Ms. Erika D. Salley, City Clerk.

AUDIT COMMITTEE MEETING

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that the purpose of this meeting is to comply with the professional standards in order to encourage two way communication between the external audit firm and the individual charged with governance (Audit Committee / City Council) to see if there are any particular areas of concern with the city's finances; areas you may want us to look at; are you aware of any fraudulent activities or allegations of fraud.

Mayor Coble said that the Audit Committee was a suggestion of the business community that we asked to help us. He said that we can figure out how this committee would work once we get the audits and monthly reports on track.

▪ **Mr. Finlay joined the meeting at 2:31 p.m.**

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that the Council should focus on high risk areas. He asked how employees go about reporting their concerns without fear of retribution. He believes that the Council members would say yes we have an ethical policy and would not tolerate anybody taking unfavorable action against somebody doing something right, but down in the trenches that's not the way it is viewed.

Councilor Sinclair asked if people are saying that or is that typical.

Mr. Bud Addison, Audit Senior Manager for of Webster Rogers, LLP said that most times it is not the external auditor that uncovers fraud. Most people say they don't know how to report fraud or that no one asked them about it.

Mr. Charles P. Austin, Sr., City Manager said that he has seen long-term employees who have made similar statements. They will tell you things, but don't want it to be known that they said it for fear of retribution.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that the attitude in the Finance Department has improved over the last 4 months. The memo that was sent via e-mail to the City Manger at the end of 2007 indicated that the financial statements would be ready by mid-January 2008, but people in finance knew that could not happen all along and were not able to communicate that to a level of management that could take action.

Councilor Finlay asked how the Council would design a policy that prevents us from lagging behind in financial data. He recalled a letter that he submitted to the Council in regards to the financial situation, noting that no one took it seriously and that one individual told him not to give them such information, because it is covered under the Freedom of Information Act (FOIA).

Councilor Sinclair said that we could talk about that or we could focus on the audit. She responded that she took Mr. Finlay's letter very seriously and so did others and they raised issues and grilled the City Manager over and over again.

Councilor Finlay noted that it is now 18 months later and we haven't advanced the ball from a timeline point of view. He said that next years audit may be on time, but the Council needs to develop a policy wherein they have fiduciary responsibility to do something when these issues are raised.

Councilor Rickenmann said that Mr. Finlay's point is well taken and now we will have an Audit Committee that will meet on a regular basis. This is where these issues need to come. I will do everything in my power to be here for the meetings and I will do the same thing with the budget meetings in September so that we are working forward and not backward. It would be helpful to know where we are now in the audit process and if we are going to hit these targets. The former Finance Directors and auditors led us to believe that we were in a much safer haven than we were. From a financial standpoint we want to know if our finances are straight and that our numbers are accurate. He suggested that they schedule another meeting to go through questions and suggestions.

Councilor Finlay said that the Council has to set a very clear policy to the City Manager and staff. We have to be proactive and when we get put on notice we must do our fiduciary responsibility.

Ms. Missy Caughman, Interim Finance Director explained that in terms of the audit, they have committed to June 30, 2008 and they are on track with getting all of the tasks done. She noted that they still need to review capital assets.

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina said that the project has three (3) parts to it; they are on the preparation side doing the financial statements. Mr. Don Mobley is preparing the 2006/2007 statements; and Mr. Addison is doing the audit of the 2006/2007 financials. There are two other parts to the entire project; one part was reorganizing the entire financial staff so we can produce monthly financial statements. The current structure didn't support the objective. They needed staff with higher skill sets. The other part is that the sub ledgers are in poor condition and we are going in to redo them. For example, all of the land owned by the city doesn't match with the sub ledgers.

Councilor Finlay said that we have very little idea of what we own and what we've sold. He asked how many years have the sub ledgers been screwed up.

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina said that the errors were identified during the last audit and agreed that this has been going on for a long time.

Councilor Finlay said that in the two years he has been here they have not received an accurate monthly financial statement.

Councilor Sinclair said that it has not been easy to get financial reports. She said that they don't need them monthly statements and requested that they get them on a quarterly basis.

Mayor Coble asked how far are we now from where we need to be with the 2006/2007 audit.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP explained that his responsibility is to get the books ready so that the June 30, 2007 audit can be done and the June 30, 2007 Comprehensive Annual Financial Report (CAFR) can be issued. The biggest issue is trying to get the capital assets records. They have been working on this for four (4) months now. He said that Mr. Addison has been in for 6 weeks doing the audit on all the areas that were ready. They are looking at the CAFR that the city generated two weeks ago. He said that they will have a good draft of the CAFR for the auditor to review within a week or two and hopes that it can be issued by June 30th or a couple of weeks thereof.

Councilor Finlay asked if the audit would be ready in October.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP hopes to have an audit for fiscal year 2006/2007 in July.

Councilor Finlay asked Mr. Addison if that was a fair date.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that it is doable, if some issues get resolved. His concerns are the capital assets, because they distributed this sub ledger out to various departments and received invalid responses. For example, a back up generator for a water treatment plant was purchased in 2001 for almost \$1 million and the department reported that they did not know where it was. It could have been stolen and it should have been reported. Are you really safeguarding your assets?

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said that the generator was not stolen. He went back to that department and provided the details. They realized that they went through the list too fast and the generator was there. There are still several instances like this that are pending.

Ms. Melisa Caughman, Interim Budget Director said that this happens because of the descriptions we have are not consistent, especially when you go back 10-20 years ago.

Mayor Coble said that assuming this issue is resolved, what are the other issues?

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that he is concerned about the transfer of money, because the Internal Service Fund has significant deficits and that makes the General Fund look better than what it is. The money should have been transferred from the General Fund to cover the short falls that were caused by the under budgeting of health care costs. Even if the Council had received correct financial statements on the General Fund, he would estimate that the General Fund is understated by \$15 to \$16 million.

Councilor Finlay said that we have been under funding pensions and health insurance to leave more cash flow in the General Fund. We have significant unfunded liabilities on our balance sheet to pension and healthcare.

Councilor Sinclair said that this is not new information.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP explained that last year the fund balance number in the audit was positive, but this year there was another big loss and the fund balance number is negative. There was a significant loss in 2006 and 2007, because of risk management related matters such as healthcare claims and law suits.

Councilor Rickenmann asked how this is covered.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that it's getting paid, but not out of the General Fund. He noted that the General Fund will have to ultimately assume the liability.

Councilor Rickenmann asked why we haven't been assigning the liability before.

Ms. Melisa Caughman, Interim Budget Director said that the losses occurred during the 2006/2007 year.

Councilor Rickenmann asked if the losses occurred in those years or if they just caught up with us during those years, because there is a big difference.

Ms. Melisa Caughman, Interim Budget Director responded that the law suits occurred during those years.

Councilor Sinclair noted that healthcare is an on-going issue, but lawsuits are one shot deals. She said that this isn't a surprise but we must be clear about the source of the problem.

Councilor Finlay said that the problem is the consistency of the lawsuits and that the urgency of the situation is compounded by the fact that we found out years later.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that financial statements focus on the General Fund; therefore, this issue would not have shown up unless someone reported a problem within the Internal Service Fund.

Councilor Finlay asked for the fund balances this morning and he asked for the fund balances three (3) months ago. He said that it is easy to make an income statement look good if you don't know what your liabilities and assets are.

Councilor Sinclair asked what the Council needs to focus on in terms of this meeting.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that the focus should be on the need for financial information; how does someone communicate a problem; beefing up the internal auditor position; the need for an internal audit manager that is a C.P.A. and works with the Audit Committee; and follow an audit schedule, provide reports and issues that are found. The Audit Committee would address those issues found during the audits.

Councilor Rickenmann asked how we go about auditing the auditor.

Ms. Melisa Caughman, Interim Budget Director said that's the external auditor's job.

Councilor Rickenmann asked what checks and balances can we put into place, once we address the situation.

Ms. Wanda Charing Certified Public Accountant / Consultant for the Municipal Association of South Carolina explained that three (3) internal audit positions are needed to audit every area of the city throughout the year and would report back to the Audit Committee with their findings.

Councilor Sinclair asked if the budget reflected the recommendations for three (3) positions.

Mr. Charles P. Austin, Sr., City Manager said that there are two (2) budgeted positions for an Internal Auditor, but one (1) is currently vacant.

Councilor Finlay asked how we fix the \$16 million deficit in the Risk Management Fund.

- **Mr. Davis arrived at 3:05 pm.**

Councilor Rickenmann asked if the money had been allocated or spent.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP explained that the actual insurance claims are real dollars, but some of the law suits are estimates that have accrued.

Councilor Finlay asked how much was booked for the hotel litigation.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP replied \$4 million.

Councilor Rickenmann asked for the numbers for healthcare and litigation.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP explained that \$7 million was booked for legal and approximately \$9 million has been spent on healthcare.

Councilor Rickenmann said that we need to know our fund balances and liabilities for the Risk Management Fund; I don't know how we can vote on a budget next week without knowing the balances.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP urged the Council to not get confused with the GASB 45 and the liability issue. This is cash the city has already spent, not actuarial and it is not related to GASB 45. He said that the general ledger in IFAS has shown the deficit as it occurred.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said that the city had a \$10 million loss in the prior year and another big one in 2007 for all claims.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP clarified that the city will have to transfer expenses from the Internal Service Fund to the General Fund, thus reducing the fund balance.

Ms. Melisa Caughman, Interim Budget Director said that at the end of 2006 we had a \$24 million General Fund balance.

Councilor Rickenmann stated that a good portion of that fund balance is already booked out.

Ms. Melisa Caughman, Interim Budget Director said that some of it is encumbered. There have been some recommendations for allocations from the fund balance, but no official action has been taken.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said that the unrestricted fund balance for the General Fund as of June 30, 2006 is \$22.3 million.

Mayor Coble said that the General Fund balance is coming way down.

Ms. Melisa Caughman, Interim Budget Director said that the fund balance will go up.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said that the fund balance will go up in the General Fund, but the Internal Service Fund will go down.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP is concerned that the Internal Service Fund has shown a significant deficit for the past two years. Have you budgeted enough this year to cover that shortfall?

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP explained that last year the city lost \$11 million in the Internal Service Fund.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP anticipates that the city will lose another \$11 million for health insurance for fiscal year 2007/2008.

Ms. Melisa Caughman, Interim Budget Director explained that in 2007/2008 we budgeted an additional \$1 million and another \$1 million for this current year out of the General Fund and some from the Water and Sewer Fund.

Councilor Rickenmann asked how do we clean this up and get a true net fund balance.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that this has happened for two years in a row and unless you have significantly budgeted more for 2007/2008 than you did for 2006/2007, you will have another \$10 or \$11 million deficit.

Councilor Finlay suggested that they look at the budget and dramatically cut expenditures next year, because they can't raise taxes. If not, we will wipe out the entire reserves in three (3) years.

Ms. Melisa Caughman, Interim Budget Director said that we also need to make changes to our benefits coverage. In 2002/2003 the claims were \$8 million and now they are \$16 million since health insurance has risen over the years across the country.

Councilor Rickenmann asked what other liabilities do we have outstanding.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said that it is a lot of little things.

Councilor Finlay asked how much accrued vacation time do we have as a liability. We have to understand that \$4.5 million has built up as a liability. We need to develop a policy that cuts that liability off in the future.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that the accrued vacation time won't be paid all at once. The budget is fine and the budget process is fine, but the information system that is not in place prohibits the Council from knowing the true cost of health care benefits.

Mayor Coble said that in July we can say that we are making a decision based on the available information and that the budget year has started, but we may have to make adjustments in everything that we spend. We need to talk about reducing the liabilities for healthcare and what has already been spent is most likely to be covered by existing surpluses, but we can't have it continue year in and year out.

Councilor Rickenmann said that it sounds like the idea of paying down debt is out the window.

Councilor Finlay said that the budget is built on quicksand and that it is embarrassing and a colossal waste of everyone's time.

Councilor Sinclair disagreed with Mr. Finlay's statement.

Ms. Melisa Caughman, Interim Budget Director explained that the budget is based on projections; the revenues are realistic, but the Council needs to decide whether or not to reallocate expenditures.

Councilor Finlay reiterated that there is a large carry forward surplus, which has never been dealt. He thinks the Council will end up using it to deal with some fund balances. There is probably 5% to 10% of our budget that we worked really hard on and we are going to have to look at redirecting that.

Mayor Coble asked if it is possible that we will have an additional unrestricted surplus from 2006/2007.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said yes and that it would be \$8 million.

Ms. Wanda Charming Certified Public Accountant / Consultant for the Municipal Association of South Carolina said that it is likely to be \$5 million.

Mayor Coble asked that they all get together, because the Council needs a more accurate picture of what needs to be done in fiscal year 2008/2009. This information is needed by Friday.

Councilor Sinclair stated that in terms of the bottom line of the budget she thinks they should let them finish their jobs and come forth with real numbers and then we can modify the budget based on that.

Councilor Finlay proposed that they ask the City Manager to get with Ms. Caughman and do a 5% reduction with funds going straight to our fund balance. This reduction should not be done across the board. Then we can move forward to deal with GASB 45 and other pension benefits.

Councilor Davis said that we don't have the solid numbers yet to know what the true deficit is.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that Council doesn't know the hard and fast numbers. He believes that the fund balance will be significantly lower by the time the Council gets hard numbers. He said that this Council is not aware of how much healthcare is costing the city. He urged the Council to pass the budget and to be cognizant of everything they spend.

Councilor Finlay suggested that they will have to increase the cost of benefits for employees and deal with GASB 45.

Councilor Rickenmann said that they needed to commit funds straight to the risk management fund and repay the TIF funds later. From a systems standpoint, who has been monitoring this and why hasn't this been brought to the Council's attention. Doesn't Blue Cross Blue Shield do an analysis upon renewal of the contract?

Ms. Melisa Caughman, Interim Budget Director said that the city last increased healthcare premiums in 2005.

Mayor Coble said that healthcare is going berserk everywhere in the United States. He asked how other governments are handling this. He supports Mr. Rickenmann's suggestion to put everything into risk management.

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina said that other cities do all of the above; they raise revenues, cut expenditures and cut employment and while most places don't increase the contribution for the employees, but they do adjust the spouse and dependents benefits.

Ms. Melisa Caughman, Interim Budget Director explained that the employee's portion is covered within the department's budget. We are trying to reduce our claims through health and wellness programs.

Council-Elect Belinda Gergel asked if the Council would begin receiving monthly financials for fiscal year 2008/2009.

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina doesn't project that they will be able to provide monthly statements until January 2009 and at that time they will deliver packages to Council and then seek feedback on what was received.

Councilor Rickenmann said that the reports should be as simple as possible. It should be a clear picture for the Council and for the public.

Council-Elect Belinda Gergel asked why it is going to take another 6 months. She asked if another team could come in to help.

▪ **Mr. Finlay left the meeting at 3:49 p.m.**

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina said that they need to train city staff and repair the sub ledgers; this is a lengthy process. There is a significant issue with cash. This requires systems and people to be in place to perform these functions. She explained that there are accountants currently working in the Finance Department and team members are added as resources are needed.

Council-Elect Belinda Gergel said that a new budget represents a new opportunity to do it right in July, but we are not set up yet to enter the data. She asked what needs to be in place for this coming year's budget in terms of how we post bills, revenues and expenditures.

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina explained that there are two (2) types of statements; an income statement and a balance sheet. Accountants focus on the balance sheet, if we can verify a balance on a balance sheet, then we know that the income statement is probably correct. She can't verify a balance on any of the balance sheets right now and she needs to get good working sub ledgers and then teach staff how to maintain them. The income statement is not significantly incorrect, but she can't verify balances on the balance sheet.

Mayor Coble asked what information could be provided in July.

- **Ms. Sinclair left the meeting at 3:54 p.m.**

Ms. Wanda Charping Certified Public Accountant / Consultant for the Municipal Association of South Carolina said that she can provide the Income Statements in August, but she can't assure that it will be accurate.

Mr. Don Mobley, Certified Public Accountant with Scott McElveen, LLP said that the cash would not be reconciled and there could be an error.

Council-Elect Belinda Gergel asked if they could provide the expenditures.

Mr. Bud Addison, Audit Senior Manager for Webster Rogers, LLP said that we can do that, but they need to do bank reconciliations first.

Mayor Coble said that it is essential for the Council to receive a report prior to January 2009. We need to say exactly what the problem is by providing a caveat. We need to start in August.

Mr. Charles P. Austin, Sr., City Manager said that the numbers that they are talking about should not have an adverse effect on us going forward with the budget.

Mayor Coble said that healthcare costs have skyrocketed, it has happened to the whole world, so it is not systemic. We are going to use a significant portion of the unallocated reserve to cover that. He recalled that the former Finance Director, Ms. Lisa Rolan told the Council about the deficit and that the reserve was going to be used to cover risk management. We have to make adjustments and develop a plan for healthcare. If we are going to cut back on the budget then we need to do so in real terms.

- **Council adjourned the Audit Committee Meeting at 4:00 p.m.**

Respectfully submitted by:

Erika D. Salley
City Clerk