Robert B. Wasserbach
County Auditor

To: Pension Board Members

From: Bob Wasserbach

Subject: Pension Board

Date: March 20, 2013

Background

In January of this year, New Castle County's external auditors, SB & Co., presented to the Pension Board the results of the Fiscal Year 2012 audit of the Pension Program's financial statements. A few of the questions asked by Board Members made the County Auditor realize that Pension Board Members may not be fully aware of the scope and limitations of such an audit.

The Pension Program audit is designed to obtain reasonable assurance that the financial statements are free of material misstatement, and the auditors' threshold for determining materiality is a high dollar amount. The audit provides an opinion on whether the financial statements present fairly, in all material respects, the net assets of the Pension Program as of the particular fiscal year-end, and the changes in its net assets for the year then ended, in conformity with generally accepted accounting principles.

Items the financial statement audit does not encompass or does not delve deeply into are as follows:

- If the auditors find exceptions in their testing, they do not usually delve deeper (and do not comment upon) the exceptions unless the dollar materiality exceeds a certain dollar amount. Thus, there could be exceptions which are symptomatic of a problem, but such exceptions are not communicated to the Pension Board (nor are they necessarily communicated to the County Auditor's Office).
- The audit opinion does not address the quality of the numbers on the financial statements. For example, if administrative expenses are $1,000,000 for a particular year, the audit will not tell you whether this amount possibly could have been less if the Program were better at managing its expenses.
- The audit does not provide an opinion on the effectiveness and efficiency of the internal controls over the all facets of the Pension Program. Although the external auditors do some analysis of internal controls, it is somewhat cursory.
- The audit does not assess the adequacy of the overall administration of the Pension Program. The audit does not look at items such as, among other things (1) whether the Pension Board has bylaws as required by County Code, (2) whether Pension Board Members have the necessary skills and expertise to adequately discharge their fiduciary responsibilities, and (3) whether the Pension Board is following best practices in the industry (e.g., GFOA Best Practices document on pension plans).
- Overall, the audit focus is financial-oriented, not operations or compliance-oriented.

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Alternatives/Suggestions

1. Have the Pension Board engage its own audit firm to audit the Pension Program's financial statements. Stipulate in the RFP that the Board wants an operational/compliance audit in addition to a financial statement audit. Please note that such audit/review will be expensive and there's a good chance there will be staff people assigned to the audit who do not have a whole lot of experience. (Current practice is that the County Auditor, in conjunction with hiring a firm to audit New Castle County's financial statements, also engages a firm to audit the Pension Program's financial statements. The same firm is typically engaged to perform both audits since the County financial statement audit also requires some audit work on the Pension Program. However, there is no reason why the Pension Board cannot engage its own audit firm to audit the Pension Program.)
2. Continue to let the County Auditor engage the audit firm for the Pension Program financial statement audit. Have the Pension Board issue a separate RFP for an external auditor/consultant to perform an operational/compliance audit, with a comprehensive review of internal controls, policies & procedures, and best practices.
3. Have the County Auditor's Office perform an operational/compliance audit, at no cost to the Pension Board, with a comprehensive review of internal controls, policies & procedures, and best practices. The County Auditor would need to obtain the approval of the Audit Committee to perform this review. Please note that the County Auditor has already begun preliminary work on such a review and has already noted several issues such as the lack of bylaws and the overall investment policy not being updated since 2008.