



1255 Imperial Avenue, #1000  
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## Agenda

### MEETING OF THE METROPOLITAN TRANSIT SYSTEM AUDIT OVERSIGHT COMMITTEE

June 14, 2012  
Executive Conference Room  
9:00 a.m.

#### ACTION RECOMMENDED

- A. 1. Roll Call
2. Approval of the Minutes of October 20, 2011 ~~21~~ Approve
- B. COMMITTEE DISCUSSION ITEMS
1. Audit Engagement Letter (Tom Lynch) Possible  
Action would review the audit engagement letter. Action
2. Interim Audit (Tom Lynch) Receive  
Action would receive a report on: (1) interim audit work conducted by Pun and McGeady (MTS's independent auditor); and (2) related observations coupled with management's responses.
3. Contract for Audit Services - Status (Tom Lynch) Possible  
Action would receive a report and provide direction to the staff regarding the upcoming Request for Proposals (RFP) for audit services. Action
4. Audit Schedule (Tom Lynch) Possible  
Action would review the audit schedule. Action
5. FY 12 Audit Plan Update and Preliminary FY 13 Audit Plan (Daniel Madzellan) Possible  
Action would receive a status report on the FY 12 audit plan as well as a preliminary audit plan for FY 13. Action
- C. COMMITTEE MEMBER COMMUNICATIONS AND OTHER BUSINESS
- D. PUBLIC COMMENTS
- E. NEXT MEETING DATE: To be determined.
- F. ADJOURNMENT

Please SILENCE electronics  
during the meeting



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Metropolitan Transit System (MTS) is a California public agency comprised of San Diego Transit Corp., San Diego Trolley, Inc., San Diego and Arizona Eastern Railway Company (nonprofit public benefit corporations), and San Diego Vintage Trolley, Inc., a 501(c)(3) nonprofit corporation, in cooperation with Chula Vista Transit. MTS is the taxicab administrator for seven cities. MTS member agencies include the cities of Chula Vista, Coronado, El Cajon, Imperial Beach, La Mesa, Lemon Grove, National City, Poway, San Diego, Santee, and the County of San Diego.

AUDIT OVERSIGHT COMMITTEE MEETING FOR THE  
METROPOLITAN TRANSIT SYSTEM (MTS),  
1255 Imperial Avenue, Suite 1000  
San Diego, CA 92101

October 20, 2011

MINUTES

A. ROLL CALL

1. Chairman Ewin called the meeting to order at 9:35 a.m. A roll call sheet listing Audit Oversight Committee member attendance is attached.

2. APPROVAL OF MINUTES

Mr. Minto moved for approval of the minutes of the August 11, 2011, Audit Oversight Committee meeting. Mr. Ovrom seconded the motion, and the vote was 5 to 0 in favor.

B. AUDIT OVERSIGHT COMMITTEE DISCUSSION ITEMS

1. Draft 2011 Comprehensive Annual Financial Report (CAFR)

Linda Musengo, Finance Manager, provided a draft of the Comprehensive Annual Financial Report (CAFR) to the Committee. She stated that there will be no significant financial changes from the 2010 CAFR.

She explained that on page A-23 the change in short term liabilities with the significant increase of \$13 million, Accounts Payable number is higher due to timing issues. On page A-24 current year operating statement is remarkably well, the only significant change in operations is expense was flat, decrease in subsidy revenue is related to Transnet, MTS received a large amount of money last year due to the acquisition of the trolley cars and MTS did not receive the money this year.

The Audit Oversight Committee engaged in a discussion regarding the single audit requirements, GASB study, Fiscal Sustainability Projection and the great cooperation that the MTS staff provided with completing the report.

Mr. Ewin referenced pages for review:

- A-7 Mission Statement,
- A-9 Awards Acknowledgement,
- A-13 MTS Executive Level Organization Chart,
- A-29 Table of Contents with the list of notes,
- A-29 Note 9 Commodity Swap: Ms. Musengo explained the Commodity Swap,
- A-37 GASB Pronouncements; Ms. Musengo explained the new GASB Pronouncements,
- A50 Pending Legal Actions; Mr. Ewin asked is there anything that the committee should be concern about. Ms. Landers stated that she is not sure of the event status and will continue to follow up.
- A51 Post Employment Health Care Benefits,
- A59 Unfunded Liabilities,

- A61 SDTC Unfunded Liability,
- A93 Fare Structure,
- A97 Ratio of Outstanding Debts and,
- A99 Regional Population & Personal Income Statistics.

Mr. Ewin requested that he would like to review final CAFR before presenting to the full Board in November.

Action Taken

Mr. Minto moved to receive a report on the Draft FY 2010 CAFR for review and discussion. Mr. Ovrom seconded the motion, and the vote was 5 to 0 in favor.

C. COMMITTEE MEMBER COMMUNICATIONS AND OTHER BUSINESS

There were no Committee communications.

D. PUBLIC COMMENTS

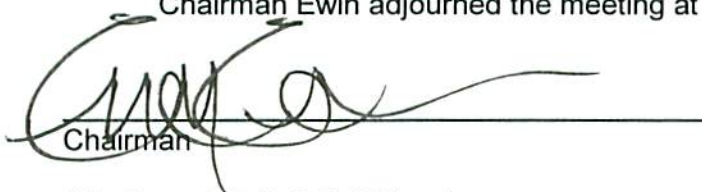
There were no public comments.

E. NEXT MEETING DATE

The next meeting will be held as called.

F. ADJOURNMENT

Chairman Ewin adjourned the meeting at 10:04 a.m.



Chairman

Attachment: Roll Call Sheet



**AUDIT OVERSIGHT COMMITTEE  
METROPOLITAN TRANSIT SYSTEM**

ROLL CALL

MEETING OF (DATE) October 20, 2011

CALL TO ORDER (TIME) 9:35 a.m.

RECESS \_\_\_\_\_

RECONVENE \_\_\_\_\_

CLOSED SESSION \_\_\_\_\_

RECONVENE \_\_\_\_\_

ADJOURN 10:04 a.m.

BOARD MEMBER (Alternate)	PRESENT (TIME ARRIVED)	ABSENT (TIME LEFT)
EWIN (Chair) <input checked="" type="checkbox"/>		
YOUNG <input checked="" type="checkbox"/> (Lightner) <input type="checkbox"/>		
MATHIS <input checked="" type="checkbox"/>		
OVROM <input checked="" type="checkbox"/> (Janney) <input type="checkbox"/>		
ROBERTS <input type="checkbox"/> (Cox) <input checked="" type="checkbox"/>		
MINTO <input checked="" type="checkbox"/> (Cunningham) <input type="checkbox"/>		
Transportation Committee Rep Slot (Mathis)		

SIGNED BY OFFICE OF THE CLERK OF THE BOARD: 

CONFIRMED BY OFFICE OF THE GENERAL COUNSEL: 



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## Agenda Item No. B1

### MEETING OF THE METROPOLITAN TRANSIT SYSTEM AUDIT OVERSIGHT COMMITTEE

June 14, 2012

#### SUBJECT:

AUDIT ENGAGEMENT LETTER (TOM LYNCH)

#### RECOMMENDATION:

That the MTS Audit Oversight Committee review the audit engagement letter (Attachment A).

#### Budget Impact

None at this time.

#### DISCUSSION:

#### Review and Approval of the Audit Engagement Letter

Auditing standards require the auditor to present a written engagement letter and obtain a signature from an officer of the company. Attached is the engagement letter from Pun & McGeady for the FY 2012 audit. A representative from Pun & McGeady will be available for questions.

Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Tom Lynch, 619.557.4538, [tom.lynch@sdmts.com](mailto:tom.lynch@sdmts.com)

JUNE14-12.B1.AUDIT ENGAGEMENT LTR.TLYNCH

Attachment: A. Audit Engagement Letter dated 4/2/12





Att. A, AI B1, 6/14/12  
4225 Executive Square  
Suite 1070  
San Diego, California 92037  
**Phone:** 855.276.4272  
**Fax:** 855.276.5214  
[www.pm-llp.com](http://www.pm-llp.com)

April 2, 2012

Board of Directors  
**San Diego Metropolitan Transit System**  
1255 Imperial Avenue, Suite 1000  
San Diego, California 92101

**RE: Engagement of Pun & McGeady LLP (the "Firm") as MTS' Independent Auditors**

We are pleased to confirm our understanding of the services we are to provide to the San Diego Metropolitan Transit System ("MTS") for the year ending June 30, 2012. The Firm's services are provided pursuant to MTS Contract No. G1013.0-06, as modified by G1013.1-06 (exercise of extension options) ("Contract"). Nothing in this engagement letter is intended to modify or amend the terms and conditions set forth in the Contract. In the event a conflict arises between this letter and the Contract, the terms in the Contract shall prevail.

**Fiscal Year 2011/12 Audit Assignment**

We will audit the financial statements of the business-type activities which collectively comprise the basic financial statements of MTS as of and for the year ending June 30, 2012. Accounting standards generally accepted in the United States provide for certain required supplementary information (RSI), such as management's discussion and analysis (MD&A), to accompany MTS' basic financial statements. As part of our engagement, we will apply certain limited procedures to MTS' RSI. These limited procedures will consist principally of inquiries of management regarding the methods of measurement and presentation, which management is responsible for affirming to us in its representation letter. Unless we encounter problems with the presentation of the RSI or with procedures relating to it, we will disclaim an opinion on it. The following RSI is required by generally accepted accounting principles and will be subjected to certain limited procedures, but will not be audited:

- 1) Management's Discussion and Analysis
- 2) Schedule of Funding Progress - Pensions
- 3) Schedule of Funding Progress - OPEB

Supplementary information other than RSI also accompanies MTS' basic financial statements. We will subject the following supplementary information to the auditing procedures applied in our audit of the basic financial statements and will provide an opinion on it in relation to the basic financial statements:

- 1) Schedule of Expenditures of Federal Awards
- 2) Combining Financial Statements
- 3) Individual Fund Financial Statements and Schedules



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The following other information accompanying the financial statements will not be subjected to the auditing procedures applied in our audit of the financial statements, and for which our auditor's report will not provide an opinion or any assurance.

- 1) Introductory Section
- 2) Statistical Section

#### Audit Objectives

The objective of our audit is the expression of opinions as to whether your basic financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles and to report on the fairness of the supplementary information referred to in the second paragraph when considered in relation to the financial statements as a whole. The objective also includes reporting on —

- Internal control related to the financial statements and compliance with laws, regulations, and the provisions of contracts or grant agreements, noncompliance with which could have a material effect on the financial statements in accordance with Government Auditing Standards.
- Internal control related to major programs and an opinion (or disclaimer of opinion) on compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a direct and material effect on each major program in accordance with the Single Audit Act Amendments of 1996 and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

The reports on internal control and compliance will each include a statement that the report is intended solely for the information and use of management, the body or individuals charged with governance, others within the entity specific legislative or regulatory bodies, federal awarding agencies, and if applicable, pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Our audit will be conducted in accordance with auditing standards generally accepted in the United States of America; the standards for financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; the Single Audit Act Amendments of 1996; and the provisions of OMB Circular A-133, and will include tests of accounting records, a determination of major program(s) in accordance with OMB Circular A-133, and other procedures we consider necessary to enable us to express such opinions and to render the required reports. If our opinions on the financial statements or the Single Audit compliance opinions are other than unqualified, we will discuss the reasons with you in advance. If, for any reason, we are unable to complete the audit or are unable to form or have not formed opinions, we may decline to express opinions or to issue a report as a result of this engagement.

#### Audit Procedures — General

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested. We will plan and perform the audit to obtain reasonable rather than absolute assurance about whether the financial statements are free of material misstatement, whether from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the entity or to acts by management or employees acting on behalf of the entity. Because the determination of abuse is subjective, Government Auditing Standards do not expect auditors to provide reasonable assurance of detecting abuse.

Because an audit is designed to provide reasonable, but not absolute assurance and because we will not perform a detailed examination of all transactions, there is a risk that material misstatements or noncompliance may exist and not be detected by us. In addition, an audit is not designed to detect immaterial misstatements or violations



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of laws or governmental regulations that do not have a direct and material effect on the financial statements or major programs. However, we will inform you of any material errors and any fraudulent financial reporting or misappropriation of assets that come to our attention. We will also inform you of any violations of laws or governmental regulations that come to our attention, unless clearly inconsequential, and of any material abuse that comes to our attention. We will include such matters in the reports required for a Single Audit. Our responsibility as auditors is limited to the period covered by our audit and does not extend to any later periods for which we are not engaged as auditors.

Our procedures will include tests of documentary evidence supporting the transactions recorded in the accounts, and may include tests of the physical existence of inventories, and direct confirmation of receivables and certain other assets and liabilities by correspondence with selected individuals, funding sources, creditors, and financial institutions. We will request written representations from your attorneys as part of the engagement, and they may bill you for responding to this inquiry. At the conclusion of our audit, we will require certain written representations from you about the financial statements and related matters.

#### **Audit Procedures – Internal Controls**

Our audit will include obtaining an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Tests of controls may be performed to test the effectiveness of certain controls that we consider relevant to preventing and detecting errors and fraud that are material to the financial statements and to preventing and detecting misstatements resulting from illegal acts and other noncompliance matters that have a direct and material effect on the financial statements. Our tests, if performed, will be less in scope than would be necessary to render an opinion on internal control and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to Government Auditing Standards.

As required by OMB Circular A-133, we will perform tests of controls over compliance to evaluate the effectiveness of the design and operation of controls that we consider relevant to preventing or detecting material noncompliance with compliance requirements applicable to each major federal award program. However, our tests will be less in scope than would be necessary to render an opinion on those controls and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to OMB Circular A-133.

An audit is not designed to provide assurance on internal control or to identify significant deficiencies. However, during the audit, we will communicate to management and those charged with governance internal control related matters that are required to be communicated under AICPA professional standards, Government Auditing Standards, and OMB Circular A-133.

#### **Audit Procedures – Compliance**

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will perform tests of MTS' compliance with applicable laws and regulations and the provisions of contracts and agreements, including grant agreements. However, the objective of those procedures will not be to provide an opinion on overall compliance and we will not express such an opinion in our report on compliance issued pursuant to Government Auditing Standards.

OMB Circular A-133 requires that we also plan and perform the audit to obtain reasonable assurance about whether the auditee has complied with applicable laws and regulations and the provisions of contracts and grant agreements applicable to major programs. Our procedures will consist of tests of transactions and other applicable procedures described in the OMB Circular A-133 Compliance Supplement for the types of compliance requirements that could have a direct and material effect on each of MTS' major programs. The purpose of these procedures will be to express an opinion on MTS' compliance with requirements applicable to each of its major programs in our report on compliance issued pursuant to OMB Circular A-133.



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### Management Responsibilities

Management is responsible for the basic financial statements and all accompanying information as well as all representations contained therein. Management is also responsible for identifying government award programs and understanding and complying with the compliance requirements, and for preparation of the schedule of expenditures of federal awards in accordance with the requirements of OMB Circular A-133. As part of the audit, we will assist with preparation of your financial statements, schedule of expenditures of federal awards, and related notes. You are responsible for making all management decisions and performing all management functions relating to the financial statements, schedule of expenditures of federal awards, and related notes and for accepting full responsibility for such decisions. You will be required to acknowledge in the management representation letter our assistance with preparation of the financial statements and schedule of expenditures of federal awards and that you have reviewed and approved the financial statements, schedule of expenditures of federal awards, and related notes prior to their issuance and have accepted responsibility for them. Further, you are required to designate an individual with suitable skill, knowledge, or experience to oversee any nonaudit services we provide and for evaluating the adequacy and results of those services and accepting responsibility for them.

Management is responsible for establishing and maintaining effective internal controls, including internal controls over compliance, and for evaluating and monitoring ongoing activities, to help ensure that appropriate goals and objectives are met and that there is reasonable assurance that government programs are administered in compliance with compliance requirements. You are also responsible for the selection and application of accounting principles; for the fair presentation in the financial statements of the respective financial position of the business-type activities of MTS and the respective changes in financial position and, where applicable, cash flows in conformity with U.S. generally accepted accounting principles; and for compliance with applicable laws and regulations and the provisions of contracts and grant agreements.

Management is also responsible for making all financial records and related information available to us and for ensuring that management and financial information is reliable and properly recorded. Your responsibilities also include identifying significant vendor relationships in which the vendor has responsibility for program compliance and for the accuracy and completeness of that information. Your responsibilities include adjusting the financial statements to correct material misstatements and confirming to us in the representation letter that the effects of any uncorrected misstatements aggregated by us during the current engagement and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

You are responsible for the design and implementation of programs and controls to prevent and detect fraud, and for informing us about all known or suspected fraud or illegal acts affecting the government involving (1) management, (2) employees who have significant roles in internal control, and (3) others where the fraud or illegal acts could have a material effect on the financial statements. Your responsibilities include informing us of your knowledge of any allegations of fraud or suspected fraud affecting the government received in communications from employees, former employees, grantors, regulators, or others. In addition, you are responsible for identifying and ensuring that the entity complies with applicable laws, regulations, contracts, agreements, and grants. Additionally, as required by OMB Circular A-133, it is management's responsibility to follow up and take corrective action on reported audit findings and to prepare a summary schedule of prior audit findings and a corrective action plan. The summary schedule of prior audit findings should be available for our review on June 30, 2012. You are responsible for the preparation of the supplementary information in conformity with U.S. generally accepted accounting principles. You agree to include our report on the supplementary information in any document that contains and indicates that we have reported on the supplementary information. You also agree to include the audited financial statements with any presentation of the supplementary information that includes our report thereon.



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Management is responsible for establishing and maintaining a process for tracking the status of audit findings and recommendations. Management is also responsible for identifying for us previous financial audits, attestation engagements, performance audits, or other studies related to the objectives discussed in the Audit Objectives section of this letter. This responsibility includes relaying to us corrective actions taken to address significant findings and recommendations resulting from those audits, attestation engagements, performance audits, or studies. You are also responsible for providing management's views on our current findings, conclusions, and recommendations, as well as your planned corrective actions, for the report, and for the timing and format for providing that information.

#### **Communication with Those Charged with Governance**

As part of our engagement, we are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process as well as other matters we believe should be communicated to those charged with governance. Generally accepted auditing standards do not require the auditor to design procedures for the purpose of identifying other matters to communicate with those charged with governance. Such matters include, but are not limited to, (1) the initial selection of and changes in significant accounting policies and their application; (2) the process used by management in formulating particularly sensitive accounting estimates and the basis for our conclusions regarding the reasonableness of those estimates; (3) all passed audit adjustments; (4) any disagreements with management, whether or not satisfactorily resolved, about matters that individually or in the aggregate could be significant to the financial statements or our report; (5) our views about matters that were the subject of management's consultation with other accountants about auditing and accounting matters; (6) major issues that were discussed with management in connection with the retention of our services, including, among other matters, any discussions regarding the application of accounting principles and auditing standards; (7) serious difficulties that we encountered in dealing with management related to the performance of the audit; and (8) matters relating to our independence as your auditors.

#### **Third-Party Service Providers**

We may from time to time, and depending on the circumstances, use third-party service providers in serving your account. We may share confidential information about you with these service providers, but remain committed to maintaining the confidentiality and security of your information. Accordingly, we maintain internal policies, procedures, and safeguards to protect the confidentiality of your personal information. In addition, we will secure confidentiality agreements with all service providers to maintain the confidentiality of your information and we will take reasonable precautions to determine that they have appropriate procedures in place to prevent the unauthorized release of your confidential information to others. In the event that we are unable to secure an appropriate confidentiality agreement, you will be asked to provide your consent prior to the sharing of your confidential information with the third-party service provider. Furthermore, we will remain responsible for the work provided by any such third-party service providers.

#### **Assistance By Your Personnel**

We will ask that your personnel, to the extent possible, prepare required schedules and analyses, and make selected invoices and other required documents available to our staff. This assistance by your personnel will serve to facilitate the progress of our work and minimize our time requirements.

#### **Data Collection Form**

At the conclusion of the engagement, we will complete the appropriate sections of the Data Collection Form that summarizes our audit findings. It is management's responsibility to submit the reporting package (including financial statements, schedule of expenditures of federal awards, summary schedule of prior audit findings, auditors' reports, and corrective action plan) along with the Data Collection Form to the federal audit



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clearinghouse. We will coordinate with you the electronic submission and certification. If applicable, we will provide copies of our report for you to include with the reporting package you will submit to pass-through entities. The Data Collection Form and the reporting package must be submitted within the earlier of 30 days after receipt of the auditors' reports or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audits.

#### **Independence**

Professional standards require that a firm and its members maintain independence throughout the duration of the professional relationship with a client. In order to preserve the integrity of our relationship, no offer of employment shall be discussed with any Pun & McGeary LLP professionals assigned to the audit, during the one year period prior to the commencement of the year end audit. Should such an offer of employment be made, or employment commences during the indicated time period, we will consider this an indication that our independence has been compromised. As such, we may be required to recall our auditors' report due to our lack of independence. In the event additional work is required to satisfy independence requirements, such work will be billed at our standard hourly rates. Furthermore, we strive to staff your engagement with quality, superbly trained professionals. In recognition of the extensive investment we have made to recruit and develop our personnel, we ask that you agree to the following. In the event that any of our employees accepts a position of employment with your Organization, or any of its related parties at any time while we are performing services for you or within one year thereafter, you agree to pay us a placement fee equal to the employee's annual compensation in effect on the date such employment was contracted. Such fee is payable when the employee accepts such a position.

#### **Access to Working Papers**

The audit documentation for this engagement is the property of Pun & McGeary LLP and constitutes confidential information. However, pursuant to authority given by law or regulation, we may be requested to make certain audit documentation available to U.S. Department of Transportation or its designee, a federal agency providing direct or indirect funding, or the U.S. Government Accountability Office for purposes of a quality review of the audit, to resolve audit findings, or to carry out oversight responsibilities. We will notify you of any such request. If requested, access to such audit documentation will be provided under the supervision of Pun & McGeary LLP personnel. Furthermore, upon request, we may provide copies of selected audit documentation to the aforementioned parties. These parties may intend, or decide, to distribute the copies or information contained therein to others, including other governmental agencies.

The audit documentation for this engagement will be retained for a minimum of seven years after the report release or for any additional period requested by the U.S. Department of Transportation, Oversight Agency for Audit, or Pass-through Entity. If we are aware that a federal awarding agency, pass-through entity, or auditee is contesting an audit finding, we will contact the party(ies) contesting the audit finding for guidance prior to destroying the audit documentation.

The Firm is required to undergo a "peer review" every three years. During the course of a Peer Review engagement, selected working papers and financial reports, on a sample basis, will be inspected by an outside party on a confidential basis. Consequently, the accounting and/or auditing work we performed for you may be selected. Your signing this letter represents your acknowledgement and permission to allow such access should your engagement be selected for review.

As a result of our prior or future services to you, we may be required or requested to provide information or documents to you or a third-party in connection with a legal or administrative proceeding (including a grand jury investigation) in which we are not a party. If this occurs, our efforts in complying with such request or demands will be deemed a part of this engagement and we shall be entitled to compensation for our time and



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reimbursement for our reasonable out-of-pocket expenditures (including legal fees) in complying with such request or demand. This is not intended, however, to relieve us of our duty to observe the confidentiality requirements of our profession.

#### Other Services

We are always available to meet with you and/or other management personnel at various times throughout the year to discuss current business, operational, accounting and auditing matters affecting your Organization. Whenever you feel such meeting are desirable please let us know; we are prepared to provide services to assist you in any of these areas.

#### Timeline

We expect to begin our audit on approximately April 9, 2012 and to issue our reports no later than December 31, 2012.

Kenneth H. Pun, CPA is the engagement partner and is responsible for supervising the engagement and signing the reports or authorizing another individual to sign them.

#### Report Distribution and Other

We will provide copies of our reports to MTS; however, management is responsible for distribution of the reports and the financial statements. Unless restricted by law or regulation, or containing privileged and confidential information, copies of our reports are to be made available for public inspection.

#### Most Recent External Quality Control Review

*Government Auditing Standards* require that we provide you with a copy of our most recent external peer review report and any letter of comment, and any subsequent peer review reports and letters of comment received during the period of the contract.

Since the Firm is newly established, we have yet to have our first peer review conducted. However, the assigned engagement partner, Kenneth H. Pun, was the Partner of Caporicci & Larson, Inc. (C&L) who supervise its Southern California practice and heavily participated in the quality control process of C&L. In 2011, a quality review of the policies, practices, and procedures was conducted for Caporicci & Larson, Inc. (a subsidiary of Marcum LLP). The reviewers made an independent assessment of C&L's quality control policies and procedures and inspected the working papers and reports on a representative sample of accounting and auditing governmental clients. C&L's administrative files and records were also reviewed and our professional personnel interviewed.

After thorough study of C&L's procedures and work practices, the report had a peer review rating of pass which mean that the accounting and auditing practice of C&L has been suitably designed and complied with to provide the firm with reasonable assurance of performing and has an effective quality control system and that our accounting and auditing work conforms to professional standards.

We have scheduled our first peer review after our first anniversary and will review of the Firm's policies, practices, and procedures. The reviewers will make an independent assessment of the Firm's quality control policies and procedures and will inspect the working papers and reports on representative sample of accounting and auditing engagements. The Firm's administrative files and records will be reviewed and our professional personnel will be interviewed.



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Upon completion of our first peer review, we will furnish you the independent peer reviewers' report and the recommendations, if any.

We appreciate the opportunity to be of service to San Diego Metropolitan Transit System and believe this letter accurately summarizes the significant terms of our engagement. If you have any questions, please let us know.

Very truly yours,  
Pun & McGeady LLP

Kenneth H. Pun, CPA  
Partner

**ACCEPTED**

This letter correctly sets forth the management/auditor responsibilities and procedures for the FY 11/12 audit of the San Diego Metropolitan Transit System.

Authorized Signature: \_\_\_\_\_

Title: \_\_\_\_\_

Date signed: \_\_\_\_\_



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## Agenda Item No. B2

### MEETING OF THE METROPOLITAN TRANSIT SYSTEM AUDIT OVERSIGHT COMMITTEE

June 14, 2012

#### SUBJECT:

INTERIM AUDIT (TOM LYNCH)

#### RECOMMENDATION:

That the MTS Audit Oversight Committee receive a report on:

1. interim audit work conducted by Pun and McGeady (MTS's independent auditor);  
and
2. related observations coupled with management's responses.

#### Budget Impact

None at this time.

#### DISCUSSION:

During the month of April, Pun & McGeady conducted an interim audit and tested MTS's internal controls. Upon completion of this stage of the audit process, Pun & McGeady issued an interim status report. Management has responded to the issues raised. Both the status report and management's response are attached (Attachments A & B).

A representative from Pun & McGeady will be available to discuss the audit observations.

A handwritten signature in dark ink, appearing to read 'Paul C. Jablonski', is written over a horizontal line.

Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Tom Lynch, 619.557.4538, [tom.lynch@sdmts.com](mailto:tom.lynch@sdmts.com)

Attachments: A. Interim Status Report  
B. Management Responses to Interim Status Report







PUN & McGEADY

**San Diego Metropolitan Transit System (MTS)**  
**Fiscal Year Ended June 30, 2012**  
**Interim Status Report**  
**April 30, 2012**

**INTERIM AUDIT PROCEDURES:**

The purpose of our interim audit was to gain an understanding of how MTS' internal control systems are designed and implemented in order to prevent and detect material misstatements, to evaluate the effectiveness of those controls designed and implemented to achieve these goals, and to determine if opportunities for strengthening internal controls existed. To accomplish this, we interviewed management and staff regarding policies and procedures, performed walkthroughs of significant transactions cycles, identified key controls, and, in certain instances, designed tests to evaluate the operating effectiveness of key internal controls in the following significant transaction cycles:

- Financial Reporting
- Revenues and Cash Receipts for SDTI and SDTC
- Expenditures and Cash Disbursements
- Payroll and Related Liabilities
- Inventory
- Capital Assets

In addition to updating our understanding of MTS' internal control system, we also performed procedures to evaluate MTS' Information Technology (IT) system and fraud risk.

**CURRENT YEAR END RESULTS AND DISCUSSION ITEMS:**

Based on the interim procedures performed, internal controls for the selected transaction cycles appeared to be both properly designed and effectively operating in order to prevent and detect material misstatements. We found no instances based our testing that indicated internal controls were not operating effectively.

However, during the course of fieldwork we noted MTS was experiencing major IT issues with its shared database and IT system. Through interview and observation we saw instances where files and applications were in the process of being recovered and instances of data loss. This issue raises the following concerns for our year procedures:

- The extent of data loss, particularly with ridership information used for National Transit Database reporting and how this potentially affects our ability to perform the related Agreed-Upon Procedures



- Delays in preparation of year end schedules and reports if files need to be recreated.

These are issues we will be following up on as we prepare for the 2012 year end audit.

#### REPORTS TO BE ISSUED

We will perform the following audits and agreed upon procedures enumerated below for the year ended June 30, 2012. Our audit will be conducted in accordance with U.S. generally accepted auditing standards, the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America.

1. Comprehensive Annual Financial Report
2. Single Audit
3. SDTC Employees' Retirement Plan
4. Transportation Development Act (TDA)
5. National Transit Database (NTD)
6. Prop 1B PTMISEA
7. Indirect Cost

#### YEAR END FIELDWORK DATE

We are scheduled to begin fieldwork August 27, 2012.





Att. B, AI B2, 6/14/12

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San Diego, CA 92101-7490  
(619) 231-1466 • FAX (619) 234-3407



May 17, 2012

Ken Pun  
Pun & McGeedy  
4225 Executive Square, Suite 1070  
San Diego, CA 92037

Dear Mr. Pun:

This letter provides management responses to the issues raised in the Interim Status Report for the audit of FY 2012.

### Issues

Based on the interim procedures performed, internal controls for the selected transaction cycles appeared to be both properly designed and effectively operating in order to prevent and detect material misstatements. We found no instances based our testing that indicated internal controls were not operating effectively.

However, during the course of fieldwork we noted MTS was experiencing major IT issues with its shared database and IT system. Through interview and observation we saw instances where files and applications were in the process of being recovered and instances of data loss. This issue raises the following concerns for our year procedures:

- The extent of data loss, particularly with ridership information used for National Transit Database reporting and how this potentially affects our ability to perform the related Agreed-Upon Procedures
- Delays in preparation of year end schedules and reports if files need to be recreated.

### Management Responses

#### Generally on the loss of data

On Friday, March 23, 2012, MTS suffered a catastrophic failure of our enterprise data storage infrastructure. Technical support from EMC, the manufacturer of the enterprise storage hardware, was immediately engaged to attempt to resolve the failures and preserve as many of our systems and as much of our data as possible. While these efforts were ultimately successful in repairing and/or replacing failed hardware, EMC was unable to preserve the files systems and data housed in this storage. This event resulted in the loss of a significant amount



San Diego Metropolitan Transit System  
Management Responses to Interim Audit Report  
May 17, 2012

critical MTS data. Given the configuration of MTS's enterprise data storage infrastructure, the above failure also lost a significant amount of MTS's backup files.

IT staff attempted to restore as much backup data as could be found on media that was separate from the enterprise storage infrastructure disks. As part of this effort, outside expertise was utilized. With this expert assistance, data was recovered to the full extent possible; however, it has been determined and verified that MTS has suffered a significant loss of data.

In working with outside expertise, MTS has received a recommendation to guard against a reoccurrence of losing critical data. This involves hardware improvements, configuration changes, and process changes. MTS is currently in the process of implementing these changes.

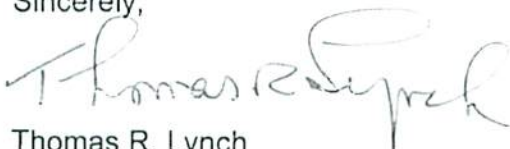
Regarding completion of the National Transit Database reporting and related Agreed-Upon Procedures

Operational data for the National Transit Database (NTD) is compiled from a number of sources. At this point, it appears that all of these sources are either not housed within the recently failed storage infrastructure, have been recovered from backup, or have been recreated by project managers. We don't anticipate any major disruptions in the availability or quality of data for the FY2012 NTD report.

Delays in preparation of year end schedules and reports if files need to be recreated

The data that was lost in the shared files were primarily Excel and Word files staff uses for creating support schedules, budgeting, and other analysis. No data from core accounting systems was lost. As such MTS anticipates no delays in preparation of schedules or reports used for the year end audit process. Finance department staff has or will recreate schedules or reports as needed staying within audit timelines.

Sincerely,

A handwritten signature in dark ink, appearing to read "Thomas R. Lynch", written over a light blue horizontal line.

Thomas R. Lynch  
Controller



MEETING OF THE METROPOLITAN TRANSIT SYSTEM  
AUDIT OVERSIGHT COMMITTEE

June 14, 2012

SUBJECT:

CONTRACT FOR AUDIT SERVICES – STATUS (TOM LYNCH)

RECOMMENDATION:

That the MTS Audit Oversight Committee receive a report and provide direction to staff regarding the upcoming Request for Proposals (RFP) for audit services.

Budget Impact

None at this time.

DISCUSSION:

The contract for audit services (MTS Doc. No. G1013.0-06) was executed between MTS and Caporicci & Larson (C&L), a subsidiary of Marcum LLP. During the past year, the principals of C&L who have managed and performed MTS's audit for the past six years (Gary Caporicci and Ken Pun) have separated from C&L and established a new partnership of Pun & McGeady. The contract between MTS and C&L has been assigned by Marcum LLP, as owner of C&L, to Pun & McGeady, with the approval of MTS. The audit for FY 2012 will be performed by Pun & McGeady under the terms of the assigned contract MTS Doc. No. G1013.0-06.

MTS's current contract for audit services began July 1, 2006, and is for five years with three 1-year options. The five base years were for audits for fiscal years 2006-2010. The option years were exercised in April 2010 and cover audits for fiscal years 2011-2013. The contract will end with the delivery of all of the compliance reports no later than March 31, 2014. A new contract needs to be in place by no later than March 31, 2014, in order to prepare for FY 2014 interim audit work, which would occur in April 2014. Below is a tentative time line of events for the RFP and contract-award process.

Request for Proposals (RFP) is issued	February 2013
Proposals to be received from audit firms	May 2013
Interviews conducted with audit firms	July 2013
Contract award brought to Audit Oversight Committee	October 2013
Contract award brought to Board of Directors	December 2013
Contract completed and signed by both parties	February 2014

Staff is seeking direction on what involvement the Audit Oversight Committee will have in the RFP and contract-award process for audit services.



Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Tom Lynch, 619.557.4538, [tom.lynch@sdmts.com](mailto:tom.lynch@sdmts.com)





Metropolitan Transit System

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## Agenda Item No. B4

### MEETING OF THE METROPOLITAN TRANSIT SYSTEM AUDIT OVERSIGHT COMMITTEE

June 14, 2012

#### SUBJECT:

AUDIT SCHEDULE (TOM LYNCH)

#### RECOMMENDATION:

That the MTS Audit Oversight Committee review the audit schedule.

#### Budget Impact

None at this time.

#### DISCUSSION:

#### Review Audit Schedule

Staff and outside auditors propose the following schedule for completion of the FY 2012 audit:

August 27-September 14	Audit field work
September 30	Draft audit report completed
October 11 – AOC	Audit progress report
November 8 – AOC	Present completed Comprehensive Annual Financial Report (CAFR)
November 15 – Board Meeting	Present completed CAFR

As always, adherence to the schedule will depend in part upon the timeliness of information from other agencies and confirmations from financial institutions and law firms. Any changes in the proposed schedule would be communicated to the Audit Oversight Committee.



Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Tom Lynch, 619.557.4538, [tom.lynch@sdmts.com](mailto:tom.lynch@sdmts.com)







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## Agenda Item No. B5

### MEETING OF THE METROPOLITAN TRANSIT SYSTEM AUDIT OVERSIGHT COMMITTEE

June 14, 2012

#### SUBJECT:

FY 12 AUDIT PLAN UPDATE AND PRELIMINARY FY 13 AUDIT PLAN  
(DANIEL MADZELAN)

#### RECOMMENDATION:

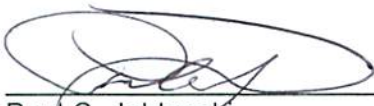
That the Audit Oversight Committee receive a status report on the FY 12 audit plan as well as a preliminary audit plan for FY 13.

#### Budget Impact

None.

#### DISCUSSION:

The MTS Internal Auditor will provide a status update on the FY 12-approved Audit Plan, which consisted of 9 internal audits and 3 consulting engagements. The Internal Auditor will also present a preliminary audit plan for FY 13 based on an estimated time budget, initial risk assessments, and management input.

  
\_\_\_\_\_  
Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Daniel Madzelan, 619.595.4920, [daniel.madzelan@sdmts.com](mailto:daniel.madzelan@sdmts.com)



# Audit Oversight Committee Meeting

## MTS Internal Audit

### FY12 Audit Plan Update & First Draft of FY13 Plan

Daniel Madzelan

June 14, 2012



### FY12 Approved Audit Plan

Operation	Primary Business Unit	Audit Type	Risk Impact	Risk Likelihood	Estimated Hours
<u>Significant Changes in Operations Change in Control Ownership</u>					
1) Payroll	HR/Finance	Financial, Operational	High	Possible	160.0
2) Transit Store	Finance	Financial, Operational	Medium	Possible	120.0
3) Customer Service Operations	SDTC	Operational	Medium	Possible	80.0
<u>Previous Audit Follow Up Review</u>					
4) Compass Cards Risks Assessment – Control Evaluation	Finance/SANDAG	Operational	High	Possible	120.0
<u>Management Recommended (Assurance Reviews)</u>					
5) Procurement - FTA Compliance	Finance	Assurance/Compliance	High	Unlikely	160.0
6) CPUC Triennial Review (SDTI Safety)	SDTI/Security	Assurance/Compliance	High	Unlikely	120.0
<u>Farebox Controls - Revenues</u>					
7) Revenue Management	SDTI	Financial, Operational	High	Possible	120.0
8) Revenue Management	SDTC	Financial, Operational	High	Possible	80.0
<u>IT General Controls</u>					
9) System Access/Security Controls	IT (Finance)	IT, Operational	High	Possible	80.0
<u>Continuous Auditing Consulting</u>					
Warranty - LRV Maintenance Operations	SDTI	Operational	High	Near Certainty	80.0
Storeroom Ops- Trolley	Finance	Operational	High	Probable	80.0
Fraud Hotline - Governance	HR/Legal	Operational	Medium	Possible	24.0
<b>Total Estimated Hours - Scheduled Audits</b>					<b>1,224.0</b>





## FY12 Audit Plan Status Update

## Order of Performance

Audit	Status	Total Reportable Findings	High Priority Findings	Medium Priority Findings	Low Priority Finding
1) Transit Store	Completed – Report Issued	8	0	3	5
2) Revenue Management – SDTC	Completed – Report Issued	3	0	1	2
3) Revenue Management – SDTI	Completed – Report Issued	7	0	1	6
4) SDTI Safety/Security (CPUC Triennial Review)	Completed – Report Issued	4	0	1	3
5) Customer Service Operations	Completed – Report Issued	3	0	0	3
5a) Classroom Day Trip Program – Customer Service Operations	Completed – Report Issued	3	0	3	0
6) IT System Access/Security	Completed – Report Issued	7	0	3	4
7) Payroll	Final Reporting Stage	3	0	0	3
8) Procurement – FTA Compliance	Final Reporting Stage	8	0	6	2
9) Compass Cards – Follow Up	Fieldwork Stage	-	-	-	-
<b>Consultative Reviews</b>					
Fraud Hotline – Governance	Project Complete – No Audit Report	N/A	N/A	N/A	N/A
Warranty - LRV Maintenance Operations	Planning/Scope Established – Fieldwork Stage	-	-	-	-
Storeroom Ops- Trolley	Planning/Scope Established – No Fieldwork Performed	-	-	-	-
<b>TOTALS</b>		<b>46</b>	<b>0</b>	<b>18</b>	<b>28</b>



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## Audit Finding Ratings

<b>High Priority Finding</b>	<p>Immediate management attention is required. This is a serious internal control that if not mitigated could lead to:</p> <ul style="list-style-type: none"> <li>• Significant financial losses;</li> <li>• Serious violation of corporate strategies, policies, or values,</li> <li>• Reputational damage</li> <li>• Significant adverse regulatory impact (loss of operating licenses, material fines).</li> </ul>
<b>Medium Priority Finding</b>	<p>Timely management attention is required. This is an internal control that if not mitigated could lead to:</p> <ul style="list-style-type: none"> <li>• Financial losses,</li> <li>• Loss of control, non-compliance with departmental policies or procedures,</li> <li>• Adverse regulatory impact.</li> </ul>
<b>Low Priority Finding</b>	<p>Routine management attention is warranted. This is an internal control or risk finding which may lead to improvement in the quality or efficiencies of the organization or process.</p>



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## Fraud/Waste/Abuse Hotline Communication Summary

- **Total Communications - 31**
- **Total Telephone - 19**
- **Total Electronic - 12**
  
- **Department Summary**
  - SDTI - 11
  - SDTC - 8
  - Security - 6
  - Accounting/Finance - 3
  - Legal - Claims and Liability - 2
  - Planning - 1

Only one communication received involved an actual reported case of fraud. Situation involved paper day passes being bought and resold at the Pacific Fleet Trolley Station.

Information was forwarded to Security who investigated the claim. Situation is a historical problem encountered by MTS. These events should be further mitigated when paper passes are eliminated and day passes are sold exclusive on Compass Cards.



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## FY12 Audit Plan Update - Budget Comparison

Audits	Budgeted Hours/ Audit Plan	Total Actual Hours	Difference
1) Transit Store	120.0	138.0	(18.0)
2) Revenue Management – SDTC	80.0	108.5	(28.5)
3) Revenue Management – SDTI	120.0	147.0	(27.0)
4) SDTI Safety/Security (CPUC Triennial Review	120.0	132.0	(12.0)
5) Customer Service Operations	80.0	126.5	(46.5)
5a) Day Trip Program – Customer Service Operations			
6) IT System Access/Security	80.0	110.0	(30.0)
7) Payroll	160.0	146.0	14.0
8) Procurement – FTA Compliance	160.0	151.5	8.5
9) Compass Cards – Follow Up	120.0	60.0	60.0
<b>Consultative Reviews</b>			
Fraud Hotline – Governance	24.0	46.0	(22.0)
Warranty - LRV Maintenance Operations	80.0	20.0	60.0
Storeroom Ops- Trolley	80.0	4.0	76.0



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## Management Requests - Unallocated Time

- Total Time Allocated - 270 Hrs.
- Total Time Utilized - 93.5 Hrs.
- Unused Time - 176.5 Hrs.
  
- Projects
  - SDTI Special Event Revenue: Loss Event Response - 48 Hrs.
  - Buy America Audits - 34 Hrs.
  - Taxicab Elections - 11.5 Hrs.



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## Establish Time Budget Available Hours Allocation

	FY 2013	FY 2012
<b>Total Available Hours – Annual Basis</b>	<b>2,080.0</b>	<b>2,080.0</b>
Less:		
Company Holidays	72.0	72.0
Total Annual Leave Available	176.0	176.0
Training (Maintain Professional Certification)	40.0	40.0
<b>Est. Available Audit Hours</b>	<b><u>1,792.0</u></b>	<b><u>1,792.0</u></b>
Less		
<b>Audit Administration ~ 13% (Reduced from 18% previous year)</b>	<b>240.0</b>	<b>320.0</b>
FY2014 Planning and Risk Assessments		
Annual Internal Audit Quality Assessment Reviews		
General Meetings		
Fraud Hotline Administration		
<b>Unscheduled Projects/Mgmt Requests (~11%)</b>	<b>200.0</b>	<b>270.0</b>
<b>Est. Available Hours to Perform Scheduled Audits</b>	<b>1,352.0</b>	<b>1,202.0</b>



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## FY13 Audit Plan - First Draft and Est. Budget

Audit	Primary Business Unit	Audit Type	Risk Impact	Risk Likelihood	Estimated Hours
Follow Up Audits – Open Issues	Multiple Business Units	Follow Up/Assurance	Medium	Possible	220.0
Contract Compliance and Administration	Integrated Review – Multiple Business Units	External Business Relationships/ Operational Performance	High	Probable	480.0
Stores Operations	Finance	Consultative/Operational	High	Possible	240.0
Incident Response Management	Security	Operational	High	Possible	144.0
Token Management Operations	Finance	Business Process Review	High	Possible	96.0
Offsite Property (Asset) Management	Multiple Business Units	Consultative/Operational	High	Probable	88.0
Special Event Revenue Management	SDTI	Operational	High	Possible	88.0
<b>Totals – Planned Engagements</b>					<b>1,356.0</b>
<b>Est. Time Budget Available</b>					<b>1,352.0</b>
<b>Difference</b>					<b>4.0</b>



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