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## Agenda

### JOINT MEETING OF THE AUDIT OVERSIGHT COMMITTEE

for the  
Metropolitan Transit System  
San Diego Transit Corporation, and  
San Diego Trolley, Inc.

April 17, 2008

Executive Conference Room  
(Immediately following Executive Committee Meeting)

- |    |  | ACTION RECOMMENDED |
|----|--|--------------------|
| A. | 1. ROLL CALL   |                    |
|    | 2. APPROVAL OF THE MINUTES OF MARCH 6, 2008  | Approve            |
| B. | COMMITTEE DISCUSSION ITEMS   |                    |
|    | 1. <u>MTS: Audit of SDTI Revenue Collection Procedures</u><br>Action would receive a report for information. | Possible Action    |
|    | 2. <u>MTS: Audit Engagement Letter</u><br>Action would review the audit engagement letter.                   | Possible Action    |
| C. | COMMITTEE MEMBER COMMUNICATIONS AND OTHER BUSINESS   |                    |
| D. | PUBLIC COMMENTS  |                    |
| E. | NEXT MEETING DATE: To be determined.   |                    |
| F. | ADJOURNMENT  |                    |

Please turn off cell phones and pagers  
during the meeting



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

# DRAFT

## AUDIT OVERSIGHT COMMITTEE MEETING FOR THE METROPOLITAN TRANSIT SYSTEM (MTS), SAN DIEGO TRANSIT CORPORATION (SDTC), AND SAN DIEGO TROLLEY, INC. (SDTI)

March 6, 2008

MTS  
1255 Imperial Avenue, Suite 1000, San Diego

### MINUTES

#### A. ROLL CALL

1. Chairman Ewin called the meeting to order at 10:10 a.m. A roll call sheet listing Audit Oversight Committee member attendance is attached.

2. APPROVAL OF MINUTES

Ms. Atkins moved approval of the minutes of the February 14, 2008, Audit Oversight Committee meeting. Mr. Rindone seconded the motion, and the vote was 7 to 0 in favor.

#### B. AUDIT OVERSIGHT COMMITTEE DISCUSSION ITEMS

1. MTS: Appointment of Chairperson and Report on Audit Schedule (ADM 110.12)

##### ***Appointment of Chairperson:***

Chairman Ewin opened this agenda item and called for nominations from the floor. Mr. Emery nominated Mr. Ewin as Chairman of the Audit Oversight Committee. There were no other nominations.

##### Action Taken

The vote was 6 to 0 in favor, with Mr. Ewin abstaining.

##### ***Report on Audit Schedule:***

Mr. Gary Caporicci and Mr. Ken Pun of Caporicci and Larson, MTS's outside auditors, distributed four handouts; a hard copy of their Power Point presentation, the Report to Board of Directors and Management for the year ended June 30, 2007, an SAS 112 letter, and their engagement letter. Mr. Caporicci reviewed the objectives of the audit of MTS's financial statements, particularly as they apply to internal controls and material weaknesses, and their audit plan, including the scope and approach. He also reviewed management responsibilities for financial statements. He stated that they have identified two areas of high risk and high profile that will be audited – the actuarial process as well as the capital asset and payroll areas because of recent personnel changes in those two areas.

In response to a question from Mr. Monroe, Mr. Caporicci explained that the auditors do fraud detection, identify critical issues, and then do testing in these areas. Mr. Cliff Telfer, MTS Chief Financial Officer, reported that SDTC monitors cash receipts on a daily basis to make sure there are no anomalies. Mr. Peter Tereschuck, SDTI General Manager, stated that any deviations from the norm are immediately investigated.

In response to a question from Mr. Ewin, Mr. Pun explained that the external auditors review the internal auditor's plan and some of his reports. He added that they identify high risk areas and follow up on those. Mr. Caporicci confirmed that they discuss any concerns they have with management.

Mr. Caporicci also reported that there are no significant deficiencies or material weaknesses for FY ending June 30, 2007. He briefly reviewed the three control recommendations that were made by the auditors in the report. He then provided an overview of the three-page handout on Risk Assessment Standards.

Mr. Monroe reminded the auditors that Toni Atkins asked a series of questions at the December 13, 2007, Board meeting during the discussion of Comprehensive Annual Financial Report (CAFR). He requested that the external auditors answer those questions in writing during this audit. Ms. Atkins stated that Committee members should have samples of questions that they should ask themselves as follows: (1) Am I satisfied that the process followed in preparing and auditing the CAFR has been reasonably designed to produce accurate and reliable financial information; (2) do I have reason to question the integrity or the competence of members of management or outside auditors that would affect my ability to rely upon them; (3) do I know anything that would cause me to question the accuracy of the disclosures in the relative portions of the CAFR that I have reviewed or that would indicate that there is a risk that those disclosures may be misleading; and (4) in reviewing relative portions of the CAFR, are there any red flags that should be brought to the attention of management or the Audit Oversight Committee, which need further explanation. Mr. Monroe suggested Committee members also ask of the auditors "if you were sitting in my chair, knowing what you know with your technical expertise, is there any question I should ask that hasn't been asked?"

2. MTS: Audit Oversight Committee Composition (ADM 110.12)

After a brief discussion about the importance of having members on the Audit Oversight Committee with expertise in auditing and financial matters, it was agreed that Policy 22, MTS Rules of Procedure for the MTS Board, does not preclude the Committee from seating other members of the Board on the Committee in order to take advantage of such expertise. Chairman Ewin reported that his assignment on the Executive Committee will rotate to the next city at the end of this year. Ms. Lorenzen, MTS General Counsel suggested that the Ad Hoc Nominating Committee, which meets at the end of each calendar year to develop nominations for Board committees, address the composition of the AOC at its meeting at the end of this year.

Mr. Emery pointed out that if the Board simply adds a person with specific expertise to the composition of the AOC, it will then have a quorum of the Board.

Action Taken

There was no action taken.

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 11:00 a.m.

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Chairman

Attachment: A. Roll Call Sheet  
gail.williams/minutes

**AUDIT OVERSIGHT COMMITTEE  
METROPOLITAN TRANSIT SYSTEM**

ROLL CALL

MEETING OF (DATE) 3/6/08

CALL TO ORDER (TIME) 10:10 a.m.

RECESS \_\_\_\_\_

RECONVENE \_\_\_\_\_

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

RECONVENE \_\_\_\_\_

ADJOURN 11:00 a.m.

BOARD MEMBER (Alternate)	PRESENT (TIME ARRIVED)	ABSENT (TIME LEFT)
ATKINS <input checked="" type="checkbox"/> (Young) <input type="checkbox"/>		
EMERY <input checked="" type="checkbox"/> (Cafagna) <input type="checkbox"/>		
EWIN <input checked="" type="checkbox"/> (Clabby) <input type="checkbox"/>		
MATHIS <input checked="" type="checkbox"/>		
MONROE <input checked="" type="checkbox"/> (McLean) <input type="checkbox"/>		
RINDONE <input checked="" type="checkbox"/> (McCann) <input type="checkbox"/>		
ROBERTS <input type="checkbox"/> (Cox) <input checked="" type="checkbox"/>		

SIGNED BY OFFICE OF THE CLERK OF THE BOARD

Gail Williams

CONFIRMED BY OFFICE OF THE GENERAL COUNSEL:

[Signature]



Metropolitan Transit System

1255 Imperial Avenue, Suite 1000  
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619.231.1466, FAX: 619.234.3407

## Agenda

Item No. B1

JOINT MEETING OF THE AUDIT OVERSIGHT COMMITTEE  
for the  
Metropolitan Transit System,  
San Diego Transit Corporation, and  
San Diego Trolley, Inc.

LEG 492

April 17, 2008

SUBJECT:

MTS: AUDIT OF SDTI REVENUE COLLECTION PROCEDURES

RECOMMENDATION:

That the Audit Oversight Committee (AOC) receive a report for information.

Budget Impact

None.

DISCUSSION:

The AOC will receive an audit report by MTS's internal auditor on San Diego Trolley, Inc.'s revenue collection procedures.

Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Mark Abbey, 619.557.4573, [mark.abbey@sdmts.com](mailto:mark.abbey@sdmts.com)

APRIL17-08.AOC.B1.SDTI REV COLLECT.MABBEY.doc

Attachment: A. Audit Report of SDTI Revenue Collection Procedures



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



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## Memorandum

DATE: February 11, 2008

LEG 492 (PC 50102)

TO: Scott Donnell

FROM: Mark Abbey

SUBJECT: SDTI REVENUE COLLECTION PROCEDURES

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### EXECUTIVE SUMMARY

I have completed a review of the revenue collection process at San Diego Trolley, Inc. (SDTI). This audit was performed in accordance with the approved audit plan.

#### Audit Objectives and Scope

The objective of the review was to assess the adequacy of internal controls over the revenue collection process.

#### Observations and Recommendations

The procedures followed for revenue collection and reconciliation are well planned and generally carried out in a secure manner. Written procedures are in place for many of the revenue processes. To further improve revenue collection processes, the following recommendations are offered for management's consideration:

- Install dual combination locks on the safes.
- Regularly change the combinations on the safes.
- Counting room supervisor should review camera tapes on a regular basis.
- Periodically test ticket vending machines (TVMs) on a cyclical basis.

A detailed explanation of these recommendations is provided under "Detailed Observations."

I wish to thank Revenue Department personnel for their cooperation and assistance during the course of this review.



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## BACKGROUND

The revenue manager, who reports to the SDTI President-General Manager, supervises the SDTI revenue collection process. On an average day, over \$48,000 is collected from the TVMs. Collections from the 132 TVMs are scheduled on a weekly basis. Most bill vaults are pulled about three times each week and coin vaults once each week. A revenue collector accompanied by a security guard pulls approximately 39 vaults on a daily basis. Vaults are forwarded to the revenue facility intake room. Vaults are later counted and reconciled to the TVM vault-exchange cards. Sectran's armored car service delivers cash to the Bank of America Monday through Friday.

In addition to TVM ticket sales, special events ticket sales occur at baseball and football games and other special events. Ticket sales agents sell tickets at preassigned booths, and monies are collected at the end of the event and forwarded to the revenue facility intake room.

SDTI has developed written standard operating procedures with respect to the revenue collection process. Segregation of duties is emphasized wherever possible. The revenue facility may be relocated in the near future due to the possible sale of the existing building.

Of the 132 TVMS in service, about 107 are the new Cubic TVM models. The Cubic machines have more sophisticated capabilities and include smart card ability, which will allow passengers to utilize smart card technology.

## DETAILED OBSERVATIONS

### 1. Safes

At present, there are two safes in use in the revenue processing area. One safe is used for storage of cash removed from TVMs. The other safe is used for storage of the special events change fund. Neither safe has a dual combination lock, which would require two separate individuals to open the locks. Substantial cash is stored in each safe. For example, over a weekend, the safe containing TVM deposits may have over \$150,000 inside awaiting Monday pickup. The risk of loss is substantial since only one person can access the safe and it would be difficult to determine the specific individual involved. Requiring two different individuals to open the safes would improve control and minimize risk of loss.

In addition, I noted that the safe combinations have not been changed in many years. There are former employees who still have the combinations to these safes. The combinations should be changed on a regular routine basis in order minimize risk of theft.

### Recommendations

Install dual combination locks on the safes.

Regularly change the combinations on the safes.

### Management Response

SDTI management staff agrees that installing dual combinations on its two safes and regularly changing their combinations would improve control and minimize risk of loss. However, SDTI management staff disagrees with the assessment that it would be difficult to identify a single individual making an unauthorized entry into one of the safes. The handful of individuals capable of accessing these two safes have to go through several levels of security measures, including going through four separate doors that are monitored by digital surveillance cameras



24 hours a day/7 days a week. They would also be identified when deactivating the alarm system in both the intake and processing rooms by entering their unique personal identification number (PIN) code into the alarm panel as well as by their individual security access cards when entering these two rooms.

Grah Safe and Lock was contacted regarding both changing combinations and the availability of dual-locking safes. For approximately \$300, Grah will come out and change the combinations on both safes. For approximately \$1,000.00, Grah can remove the analog manual combination dials from both safes and replace them with digital devices that have dual-combination capability and would allow the combinations to be changed by management staff at any time. The disadvantage is that dual-combination safes would generate overtime wage increases as certain staff with the combinations would have to come in on their days off to open the safes when other staff call in sick or are on vacation. A decision will have to be made whether the cost of increased overtime wages outweighs the benefit of the marginal increases in security and control that a dual-locking safe would provide.

#### Additional Management Comments

Due to the relatively small staff size, the requirement to implement dual-combination safe locks would undoubtedly create operational issues due to days off, vacation schedules, etc. Requiring two different individuals to have separate combinations in and of itself does not prevent theft from the safe.

CCTV surveillance of the safe not only acts as a deterrent but also captures all access to the safe; however, presently revenue staff controls access to the CCTV recordings. It is therefore recommended that access to the CCTV surveillance recordings be given to the Security Department or the General Manager of Trolley. This would prevent revenue staff from potentially removing video evidence of a theft from the safe. This should be implemented in lieu of dual-combination safe locks.

#### 2. Review of Camera Videotapes

Camera coverage of the two safes in the revenue processing area has improved; however, surveillance tapes are not being reviewed on a regular basis. The counting room supervisor should routinely review surveillance tapes to ensure that standard operating procedures are followed in the counting and processing process and that no unauthorized activities occur.

#### Recommendation

Counting room supervisor should review camera tapes on a regular basis.

#### Management Response

SDTI management staff agrees that the revenue processing supervisor should review digital surveillance recordings to confirm all standard operating procedures are being followed. (Please see Standard Operating Procedure No. 101.052 and a sample video surveillance review log that specifically addresses this recommendation).

#### 3. Periodic Testing of TVMs

In reviewing documented testing procedures of the new TVMs, I noted that SDTI has fallen behind in scheduled testing of the security alarms and the revenue and ridership accuracy of the

machines. In order to ensure that the machines and security alarms are working properly, documented testing procedures should be followed on a regular basis.

#### Recommendation

Periodic testing of TVMs should be conducted on a cyclical basis.

#### Management Response

All TVM audible security alarms are tested once a week. Step 10 of the weekly TVM preventive maintenance work order for all TVMs reads "Test audible security alarm." A record of all TVM preventative maintenance work orders may be viewed in Ellipse.

SDTI management agrees that periodic testing of the TVM's revenue and ridership accuracy is a worthwhile endeavor, and the Revenue Department has fallen behind in this testing. This testing is a surprisingly time-consuming and labor-intensive process and will become even more so when credit/debit functionality is introduced. There are also security issues involved. TVM testing involves bringing cash into the field and the exchange of all cash modules before and after the test is performed. It takes at least one supervisor and another staff member a minimum of two hours to conduct a TVM test. In addition, time is required for processing staff to reset vaults, for the revenue manager to run reports, and to deduct the sales/ridership numbers generated in the test from the actual monthly totals. The time and labor costs involved in this process are not insignificant. While the department was committed to conducting this testing during the past year, staff found that it was forced to make choices between this testing and keeping the day-to-day operations running due to staffing issues.

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cc: Paul Jablonski, Tiffany Lorenzen, Cliff Telfer - MTS  
Peter Tereschuck - SDTI



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## Agenda

Item No. B2

JOINT MEETING OF THE AUDIT OVERSIGHT COMMITTEE  
for the  
Metropolitan Transit System,  
San Diego Transit Corporation, and  
San Diego Trolley, Inc.

April 17, 2008

SUBJECT:

MTS: AUDIT ENGAGEMENT LETTER

RECOMMENDATION:

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

Budget Impact

None at this time.

DISCUSSION:

Review of the Audit Engagement Letter

The audit team from Caporicci & Larson began their interim work on April 7 in connection with the FY 08 annual audit. Auditing standards require the auditor to present a written engagement letter and obtain a signature from an officer of the company. Ken Pun, engagement manager for Caporicci & Larson, will present the audit engagement letter for review.

Paul C. Jablonski  
Chief Executive Officer

Key Staff Contact: Linda Musengo, 619.557.4531, [linda.musengo@sdmts.com](mailto:linda.musengo@sdmts.com)

APRIL17-08.AOC.B2.AOC.AUDIT ENGAGEMENT LTR.LMUSENGO.doc

Attachment: A. Audit Engagement Letter







March 5, 2008

Mr. Cliff Telfer  
Chief Financial Officer  
San Diego Metropolitan Transit System  
1255 Imperial Avenue, Suite 1000  
San Diego, CA 92101-7490

Dear Mr. Telfer:

We are pleased to confirm our understanding of the services we are to provide for San Diego Metropolitan Transit System (MTS) for the year ending June 30, 2008.

We will audit the financial statements of MTS as of June 30, 2008. In addition, the audit reports we submit to you will include the Schedule of Expenditures of Federal Awards that will be subjected to the auditing procedures applied in our audit of the financial statements.

#### Audit Objectives

The objective of our audit is the expression of an opinion as to whether your 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 additional information referred to in the second paragraph when considered in relation to the financial statements taken 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 the 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, "Audit 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 for the information and use of management, 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.

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Our audit will be conducted in accordance with generally accepted auditing standards in the United States; 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 an opinion and to render the required reports. If our opinion on the financial statements or the Single Audit compliance opinion is other than unqualified, we will discuss the reasons with management in advance. If, for any reason, we are unable to complete the audit or are unable to form or have not formed an opinion, we may decline to express an opinion or to issue a report as a result of this engagement.

### **Management Responsibilities**

Management is responsible for establishing and maintaining internal control and for compliance with the provisions of contracts, agreements, and grants. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of the controls. The objectives of internal control are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, that transactions are executed in accordance with management's authorizations and recorded properly to permit the preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that federal award programs are managed in compliance with applicable laws and regulations and the provisions of contracts and grant agreements.

Management is responsible for making all financial records and related information available to us and for the accuracy and completeness of that information. We will advise management about appropriate accounting principles and their application and will assist in the preparation of MTS's financial statements, including the schedule of expenditures of federal awards, but the responsibility for the financial statements remains with management. This responsibility includes the establishment and maintenance of adequate records and effective internal controls over financial reporting and compliance, the selection and application of accounting principles, and the safeguarding of assets. Management is responsible for adjusting the financial statements to correct material misstatements and for confirming to us in the management 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. 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.

With regard to the electronic dissemination of audited financial statements, including financial statements published electronically on MTS's Internet website, management understands that electronic sites are a means to distribute information and, therefore, we are not required to read the information contained in these sites or to consider the consistency of other information in the electronic site with the original document.

### **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 assurance about whether the financial statements are free of material misstatement, whether from errors, fraudulent financial reporting, misappropriation of assets, or violations of laws or governmental regulations that are attributable to MTS or to acts by management or employees acting on behalf of MTS. As required by the Single Audit Act Amendments of 1996 and OMB Circular A-133, our audit will include tests of transactions related to major federal award programs for compliance with applicable laws and regulations and the provisions of contracts and agreements. 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 of laws or governmental regulations that do not have a direct and material effect on the financial statements or to 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. 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, tests of the physical existence of inventories, and direct confirmation of receivables and certain other assets and liabilities by correspondence with selected funding sources, creditors, and financial institutions. We will also request written representations from MTS's attorneys as part of the engagement, and they may bill MTS for responding to this inquiry. At the conclusion of our audit, we will require certain written representations from management about the financial statements and related matters.

### **Audit Procedures—Internal Control**

In planning and performing our audit, we will consider the internal control sufficient to plan the audit in order to determine the nature, timing, and extent of our auditing procedures for the purpose of expressing our opinions on MTS's financial statements and on its compliance with requirements applicable to major programs.

We will obtain an understanding of the design of the relevant controls and whether they have been placed in operation, and we will assess control risk. 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. Tests of controls relative to the financial statements are required only if control risk is assessed below the maximum level. 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 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 or material weaknesses. However, we will inform the governing body of any matters involving internal control and its operation that we consider to be significant deficiencies or material weaknesses under standards established by the American Institute of Certified Public Accountants. Any matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. We will also inform management of any control deficiencies or other matters involving internal control, if any, as required by OMB Circular A-133.

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

Our audit will be conducted in accordance with the standards referred to in the section titled Audit Objectives. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will perform tests of MTS's 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 agreements applicable to major programs. Our procedures will consist of the 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's major programs. The purpose of these procedures will be to express an opinion on MTS's compliance with requirements applicable to major programs in our report on compliance issued pursuant to OMB Circular A-133.

#### **Audit Administration, Fees, and Other**

We understand that your employees will prepare all cash, accounts receivable, and other confirmations we request and will locate any documents selected by us for testing.



At the conclusion of the engagement, we will complete the appropriate sections of and sign the Data Collection Form that summarizes our audit findings. We will provide copies of our reports to MTS; however, 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, auditor's reports, and corrective action plan) along with the Data Collection Form to the designated federal clearinghouse and, if appropriate, 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 auditor's 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 audit. At the conclusion of the engagement, we will provide information to management as to where the reporting packages should be submitted and the number to submit.

The workpapers for this engagement are the property of Caporicci & Larson and constitute confidential information. However, we may be requested to make certain workpapers available to a cognizant or grantor agency pursuant to authority given to it by law or regulation. If requested, access to such workpapers will be provided under the supervision of Caporicci & Larson personnel. Furthermore, upon request, we may provide photocopies of selected workpapers to the cognizant or grantor agency. The cognizant or grantor agencies may intend, or decide, to distribute the photocopies or information contained therein to others, including other governmental agencies.

The workpapers for this engagement will be retained for a minimum of seven years after the date the auditor's report is issued or for any additional period requested by the cognizant agencies, oversight agencies for audit, or pass-through entities. 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 workpapers.

Our fees for these services will be \$319,072 for the fiscal year ending June 30, 2008. These fees are based on anticipated cooperation from your personnel and the assumption that unexpected circumstances will not be encountered during the audit. If significant additional time is necessary, we will discuss it with you and arrive at a new fee estimate before we incur the additional costs.

Any claim or controversy arising out of the rendering of professional accounting services by Caporicci & Larson, under the terms of this agreement shall be settled by arbitration in accordance with the Rules of Practice and Procedure of Judicial Arbitration and Mediation Services, Inc. ("JAMS"). Any claim for nonpayment of amount due to Caporicci & Larson for services rendered in accordance with this agreement, however, shall be determined by a court of law, as opposed to arbitration. The agreed place of venue for any proceeding, arbitration or court, shall be San Diego, California.

Mr. Cliff Telfer  
San Diego Metropolitan Transit System  
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We will submit our bill for services on a progress basis, and billings are due upon submission. Interest is charged on balances not paid within 30 days at the rate of 1.5 percent per month. We reserve the right to suspend work and withdraw from the engagement if fees are not paid in a timely manner. It is our policy to require the fees be paid to date prior to issuing our report. If the account is not paid in full when due, you agree to pay all expenses of collection, including legal fees.

We appreciate the opportunity to be of service to you and believe this letter accurately summarizes the significant terms of our engagement. If you have any questions, please let us know. If you agree with the terms of our engagement as described in this letter, please sign the enclosed copy and return it to us.

Sincerely,  
CAPORICCI & LARSON

  
Gary M. Caporicci, CPA, CGFM  
Senior Partner

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RESPONSE:

This letter correctly sets forth the understanding of the San Diego Metropolitan Transit System.

Officer Signature: \_\_\_\_\_

Name: \_\_\_\_\_

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

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