

## SCHEDULE OF AUDIT FINDINGS AND RESPONSES

### Educational Service District No. 112 Clark County September 1, 2016 through August 31, 2017

**2017-001 The District did not report its other post-employment benefit liability in accordance with government accounting standards.**

#### *Background*

District board members, state and federal agencies, and the public rely on the information included in the financial statements and report to make decisions. District management is responsible for designing and following internal controls that provide reasonable assurance regarding the reliability of financial reporting.

While the District has an established process to perform a technical review of their financial statements, our audit identified a significant deficiency in internal controls over financial reporting that is required to be communicated under Government Auditing Standards.

#### *Description of Condition*

The District did not report the liability related to other post-employment benefits in accordance with Governmental Accounting Standards Board (GASB) Statement No. 45 – *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

#### *Cause of Condition*

When GASB Statement No. 45 took effect for governments, the District reported under a different basis of accounting. Subsequently, the District switched to reporting in accordance with generally accepted accounting principles (GAAP). The District asserts that staff evaluated GASB 45 and determined it was not applicable; however, the District did not re-evaluate its applicability in subsequent years.

#### *Effect of Condition*

The statements received for audit did not include a \$6,334,267 liability, related note disclosures and required supplementary information for other post-employment benefits.

The District subsequently obtained an actuarial study to determine the amount of liability to report, corrected the statements and prepared the required note disclosures.

### ***Recommendations***

We recommend the District:

- Perform necessary research and obtain needed actuarial studies to correctly report other post-employment benefit liabilities on its financial statements
- Establish a more formal process for performing a technical review of the financial statements to ensure they are accurately prepared and reported in accordance with generally accepted accounting principles and reporting requirements

### ***District's Response***

*The District appreciates the opportunity to respond to the finding of the State Auditor's office; we disagree with the pretext of this finding. The District maintains a process for review of generally accepted accounting principles and related reporting requirements to ensure accurate preparation and reporting of financial statements and has, in fact, researched this issue in depth and is in disagreement with the SAO regarding their position on the correct implementation of GASB Statement No. 45 (as referenced) for other post-retirement benefits (OPEB) received by retired employees through the Washington Health Care Authority (HCA).*

*GASB 45 is not a new standard; it was implemented effective with the fiscal year ending August 31, 2009 (for entities with revenues in the range of \$10m-\$100m). When the District, together with the other eight educational service districts in Washington, moved from modified cash to reporting in accordance with generally accepted accounting principles (GAAP) the SAO was involved in defining the reporting requirements and note disclosures for the educational service districts. Each GAAP requirement was reviewed with SAO representation on the committee (and with the SAO BARS manual as a benchmark) to assess impact on statements and reporting. The District has received unqualified opinions on our GAAP statements for all years since the fiscal year ended August 31, 2012 (the first year under full GAAP reporting); statements for those years have not included the*

*GASB No. 45 OPEB liability required as of this year by the SAO.*

*Further, the SAO has reported in its latest issue of its own newsletter that they discovered that "only about 20% of PEBB-member employers were correctly*

*reporting their OPEB liabilities". If 80% of the plan members have not reported a liability that SAO has suddenly determined to be appropriate after nearly 10 years of the GASB being in effect, we would argue that there is clearly a lack of clarity and definition around the appropriate implementation regarding the PEBB plan and its liabilities.*

*We have complied with the SAO's directive to implement GASB No. 45 in the presentation of the financial statements. We find it contradictory in SAO's recommendation that we establish processes for technical review of financial statements by a person who understands generally accepted accounting principles, as SAO is aware we have undergone a technical review process. The District's conclusion differs from SAO's conclusion.*

*Under Auditing Standards 1001.03, financial statements are management's responsibility. "The entity's transactions and the related assets, liabilities, and equity are within the direct knowledge and control of management. The auditor's knowledge of these matters and internal control is limited to that acquired through the audit." We had presented the financials, based on matters that we had direct knowledge and control of*

#### *Overview of Technical Research*

*Based on our research and the information available to us, including discussions with HCA personnel, we believed that the HCA OPEB plan is a cost-sharing multiple-employer plan, as defined in GASB 45:*

*A single plan with pooling (cost-sharing) arrangements for the participating employers. All risks, rewards, and costs, including benefit costs, are shared and are not attributed individually to the employers. A single actuarial valuation covers all plan members, and the same contribution rate(s) applies for each employer. [Source: GASB Implementation Guide-GASB Statements 43 and 45 on Other Postemployment Benefits, Appendix 1, Term Definitions]*

*Based on information available to management was our best judgement that the OPEB plan offered for K-12 school districts and educational service districts meet all criteria of a cost-sharing multiple employer plan and specifically did not meet criteria necessary for classification as an agent multiple employer plan, as SAO contends.*

- The plan is a single plan with pooling arrangements for participating employers*

- *All risks, rewards and costs, including benefit costs, are shared and not attributed individually to the employers*
- *A single actuarial valuation covers all plan members*
- *The same contribution rate applies for each member*
- *The plan is administered in a vehicle that is an equivalent arrangement to a trust (as defined in GASB 45)*

*Detail support for assessment of compliance with each of these criteria was assembled and made available to the SAO.*

*Management had properly recorded the contributions as required for cost-sharing plans; the GASB 45 adjustment we were required to record and reflect in our financial statements as a result of the directive of the SAO additionally recorded an actuarially-determined share of the plan's net unfunded liability, applied retrospectively. This entry was an accrual for a possible future long-term liability and did not affect cash or current operating positions.*

#### *Summary Remarks*

*In conclusion, the District feels that the financial statements were reasonably and responsibly prepared based on the preponderance of evidence available to management and the District accordingly disagrees with the finding. The best information available to management at the time indicates that the plan is a cost-sharing plan and was properly recorded in the financial statements initially presented to SAO for audit. ESD 112 appreciates the opportunity to respond.*

#### ***Auditor's Remarks***

We thank the District for its assistance during the audit and appreciate their perspective. The District, along with other Educational Service Districts (ESD) in the State of Washington, offer other post-employment benefits through a state program administered by the Health Care Authority (HCA). Once information became available that the District participated in this program, we performed a technical review of the applicability of GASB 45 that included conversations with the District, other ESDs, the HCA, and GASB. Based on our analysis, GASB 45 applies to the program offered by the District.

We look forward to working with the District again and reviewing the implementation of GASB 75 Accounting and Financial Reporting by Employers for Postemployment Benefits other than Pensions during the next audit.

#### ***Applicable Laws and Regulations***

Governmental Accounting Standards Board Statement No. 45

*Government Auditing Standards*, December 2011 Revision, paragraph 4.23 establishes reporting requirements related to significant deficiencies or material weaknesses in internal control, instances of fraud or abuse, and noncompliance with provisions of law, regulations, contracts, or grant agreements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in its *Codification of Statements on Auditing Standards*, section 265, *Communicating Internal Control Related Matters Identified in an Audit*, paragraph 7.