



**COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER**

KENNETH HAHN HALL OF ADMINISTRATION
500 WEST TEMPLE STREET, ROOM 525
LOS ANGELES, CALIFORNIA 90012-3873
PHONE: (213) 974-8301 FAX: (213) 626-5427

WENDY L. WATANABE
AUDITOR-CONTROLLER

MARIA M. OMS
CHIEF DEPUTY

ASST. AUDITOR-CONTROLLERS

ROBERT A. DAVIS
JOHN NAIMO
JUDI E. THOMAS

September 14, 2010

TO: Supervisor Gloria Molina, Chair
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

FROM: Wendy L. Watanabe
Auditor-Controller

SUBJECT: **INDEPENDENT AUDITOR'S FISCAL YEAR 2008-09 MANAGEMENT LETTER**

In conjunction with the annual audit of the County's financial statements, the independent auditor provides a Management Letter to highlight opportunities for strengthening internal controls. Attached is the Management Letter for Fiscal Year (FY) 2008-09 issued by Macias Gini & O'Connell LLP. The letter noted one finding related to contracts with the County's Workers' Compensation Third Party Administrators. The County agreed to comply with the recommendation on future contracts.

The audit report on the financial statements was previously sent to your Board and submission of this report completes the County's financial audit requirements for FY 2008-09. If you have any questions, please contact me, or your staff may contact Connie Yee at (213) 974-8321.

WLW:MMO:JN:CY:RA

Attachment

c: William T Fujioka, Chief Executive Officer
Sachi A. Hamai, Executive Officer of the Board of Supervisors
Audit Committee
Public Information Office

County of Los Angeles

Management Letter

For the Year Ended June 30, 2009

December 11, 2009

To the Honorable Board of Supervisors
County of Los Angeles, California

In planning and performing our audit of the basic financial statements of the County of Los Angeles, California, (County), for the year ended June 30, 2009, we considered the County's internal control in order to determine our auditing procedures for the purpose of expressing opinions on the basic financial statements and not to provide assurance on internal control.

However, during our audit we became aware of a certain matter that provides an opportunity for strengthening internal controls and operating efficiencies. The Management Letter that follows summarizes our comment and suggestions regarding this matter. This Management Letter does not affect the Independent Auditor's Report on the basic financial statements of the County, for the year ended June 30, 2009.

This Management Letter is intended solely for the information and use of the Board of Supervisors, the Audit Committee and County management, and is not intended to be and should not be used by anyone other than these specified parties.

We will review the status of this comment during our next audit engagement. We have already discussed this comment and suggestions with County personnel and have included the County's response to our recommendation in the attached Management Letter. We will be pleased to discuss this in further detail at your convenience, to perform any additional study of this matter, or to assist you in implementing the recommendation.

Sincerely,



Certified Public Accountants

Los Angeles, California

**COUNTY OF LOS ANGELES
MANAGEMENT LETTER
FOR THE YEAR ENDED JUNE 30, 2009**

Statement on Auditing Standards (SAS) 70 Type II Reviews and Reports

Condition

During our audit of the County's June 30, 2009 basic financial statements, we found where two of three Third Party Administrators (TPA) that handle and process transactions, specifically, workers' compensation claims, either had not undergone a Statement on Auditing Standards (SAS) 70 Type II review or the SAS 70 review did not specifically apply to the operations of the County's workers' compensation program. In context, the TPA is considered a service organization and would be subject to the provisions of SAS 70 "Reports on the Processing of Transactions by Service Organizations", and a related SAS 70 Type II report.

Per SAS 70, the above mentioned TPAs are considered service providers subject to a SAS 70 review as they perform the following duties on behalf of the County:

- Execute transactions and maintain the related accountability
- Record transactions and process related data

Criteria

SAS 70 subparagraph 8 states that if an entity uses a service organization, certain policies, procedures, and records of the service organization may be relevant to the user organization's ability to record, process, summarize, and report financial data consistent with the assertions embodied in the entity's financial statements.

SAS 70 subparagraph 12 states that a service auditor's report on policies and procedures placed in operation and tests of operating effectiveness may be relevant to a user organization's internal control structure for the following reasons:

- Whether such policies and procedures were suitably designed to achieve specified control objectives.
- Whether such policies and procedures had been placed in operation as of a specific date.
- Whether such policies and procedures that were tested were operating with sufficient effectiveness to provide reasonable, but not absolute, assurance that the related control objectives were achieved during the period specified.

Systemic or Isolated: Isolated

Cause

Currently, there is no provision in the contract between the County and the two of the three TPAs, requiring a SAS 70 review and related SAS 70 Type II report. It should be noted that the contracts with all other TPAs providing workers' compensation claims processing do contain a provision for a SAS 70 review.

**COUNTY OF LOS ANGELES
MANAGEMENT LETTER
FOR THE YEAR ENDED JUNE 30, 2009**

Recommendation

MGO recommends that the County ensure all contracts with TPAs providing workers' compensation claims processing contain a provision for a SAS 70 review and related SAS 70 Type II report. This may include amending existing contracts, where permitted.

Views of Responsible Officials and Planned Corrective Action

We agree with the recommendation and will include the SAS 70 provision in future contracts.

On February 22, 2010, MGO notified the CEO Risk Management Branch (CEO-RMB) that two third party administrators "either had not undergone a Statement on Auditing Standards (SAS) 70 Type II or the SAS 70 review did not specifically apply to operations of the County's workers' compensation program." CEO-RMB's response follows:

The County of Los Angeles contracts with Tristar Risk Management (Tristar), Intercare Insurance Services (Intercare), and Acclamation Insurance Management Services, Inc. (AIMS) for third party workers' compensation claim administration services. On September 20, 2005, the Tristar and AIMS contracts were approved. The Intercare contract was approved on September 16, 2008.

In 2006, CEO-RMB recommended the inclusion of a SAS 70 Type II provision in future workers' compensation third party administration contracts. Such a provision is included in the Intercare contract. Tristar, AIMS, and Intercare have engaged in service organization SAS 70 Type II audits.

CEO-RMB believes the inclusion of specific SAS 70 Type II requirements in third party workers' compensation claim administration service contracts is a prudent and novel industry practice. CEO-RMB staff has evaluated numerous workers' compensation claim service RFPs on the internet and contacted a number of public sector workers' compensation claims professionals (including CSAC Excess Insurance Authority) and found no evidence that SAS 70 Type II audit requirements are included in workers' compensation third party claims administration service contracts. Therefore, the CEO-RMB believes its current approach to add the SAS 70 Type II provision to new contracts is responsive to the recommendation and exceeds standard industry practices.